

DIRECTORATE-GENERAL FOR EXTERNAL POLICIES
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Trade and investments in energy in the context of the EU common commercial policy

INTA



STUDY

Trade and investments in energy in the context of the EU common commercial policy

ABSTRACT

The aim of this study is to provide a preliminary assessment of the EU legal framework for trade and investment in energy. The European economy is expected to increase its reliance on international supplies, enhancing the importance of stable and open international markets and trade relationships for its energy security. The study investigates the difference between energy policy and trade policy, the relevance of WTO provisions that may serve EU energy interests, the rules on export duties and those WTO+ provisions that affect EU energy related business. The study also analyses the relevance of bilateral trade treaties signed by the EU, with particular reference to the protection of investment following the Lisbon treaty. Finally, the study reviews the comprehensive agreements, which have been signed with the Republic of Moldova, Georgia and Ukraine.

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List of abbreviations

AA	Association Agreement
ADA	Anti-Dumping Agreement
ASCM	Agreement on Subsidies and Countervailing Measures
BIT	Bilateral Investment Treaty
BP	British Petroleum
CCP	Common Commercial Policy
CETA	Comprehensive Economic and Trade Agreement
DCFTA	Deep and Comprehensive Free Trade Area
DSB	Dispute Settlement Body
EC	European Commission
ECT	Energy Charter Treaty
EEC	European Economic Community
EEZ	Exclusive Economic Zone
EU	European Union
FDI	Foreign Domestic Investment
FET	Fair and Equitable Treatment Standard
FTA	Free Trade Agreement
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GHG	Greenhouse Gas
GPA	General Procurement Agreement
IEA	International energy Agency
IMF	International Monetary Fund
IPR	Intellectual Property Right
ISDS	Investor-State Dispute Settlement Mechanism
JODI	Joint Organisation Data Initiative
LNG	Liquefied Natural Gas
MNF	Most Favoured Nation
Mtoe	Million tonnes of oil equivalent
NAFTA	North American Free Trade Agreement
NGLs	Natural Gas Liquids
PV	Photovoltaic
RMI	Raw Materials Initiative
Toe	Tonnes of oil equivalent
TFEU	Treaty on the Functioning of the European Union
TRIMs	Agreement on Trade Related Investment Measures
TTIP	Transatlantic Trade and Investment Partnership
WTO	World Trade Organisation

1 Definition of the EU interests at stake

The European Union (EU) is the third largest consumer of energy at the global level, after China and the US. Endowed with a large population, a high level of living standards and a large industrial base, in 2013 Europe consumed 1 666 million of tonnes of oil equivalent (Mtoe), approximately 13 % of the world total. In the same year, China consumed 2 852 Mtoe (22 %), while the US consumed 2 266 Mtoe (18 %)¹.

Compared with its main competitors, the EU's economy is highly efficient: to produce one million euros of GDP, it takes 108 toe in Europe, 152 toe in the US and 351 toe in China, while the global average is 194². Moreover, improving efficiency is one of the key objectives of the EU's energy policy, with a 20 % energy efficiency target by 2020³. Low energy-intensity and increasing efficiency partially shield European economies from the negative effects of volatile or rising energy prices, but they do not eliminate a central feature of the European energy system: its dependence on imports. In 2013, 53 % of the European energy gross inland consumption was represented by imports, amounting to 877 Mtoe⁴.

Energy trade is fundamental to the competitiveness of the European economy, since substituting imported energy with an increased domestic production would raise costs. Indeed, at the current technological level, consuming only indigenously produced energy would entail a dramatic decrease in the general level of wellbeing⁵. Therefore, preserving the stability and the affordability of international supplies is of the utmost importance for the EU.

1.1 European energy trade

The composition of the energy mix and the structure of supply are the elements which determine the scope and impact of European dependence on foreign energy.

1.1.1 Composition of the energy mix

Current gross inland consumption of energy at EU level is identical to 1990 levels, approximately 1 666 Mtoe, showing a substantial decoupling between economic growth and energy demand. This trend is expected to continue in the coming decades, with gross inland consumption decreasing slightly at 1 611 Mtoe in 2030 (see Figure 1)⁶.

In addition, the composition of the energy mix has also remained relatively stable: fossil fuels dominated energy consumption in 1990 (83 %) and in 2013 (74 %), and they are still expected to represent the largest part of European energy consumption in 2030 (70 %).

¹ Eurostat [nrg_110a] and BP, *Statistical Review of World Energy*, 2014.

² Assumed exchange rate EUR/USD: 1.13. Elaboration on Eurostat [nrg_110a], BP(2014) and IMF, *World Economic Outlook Database*, October 2014.

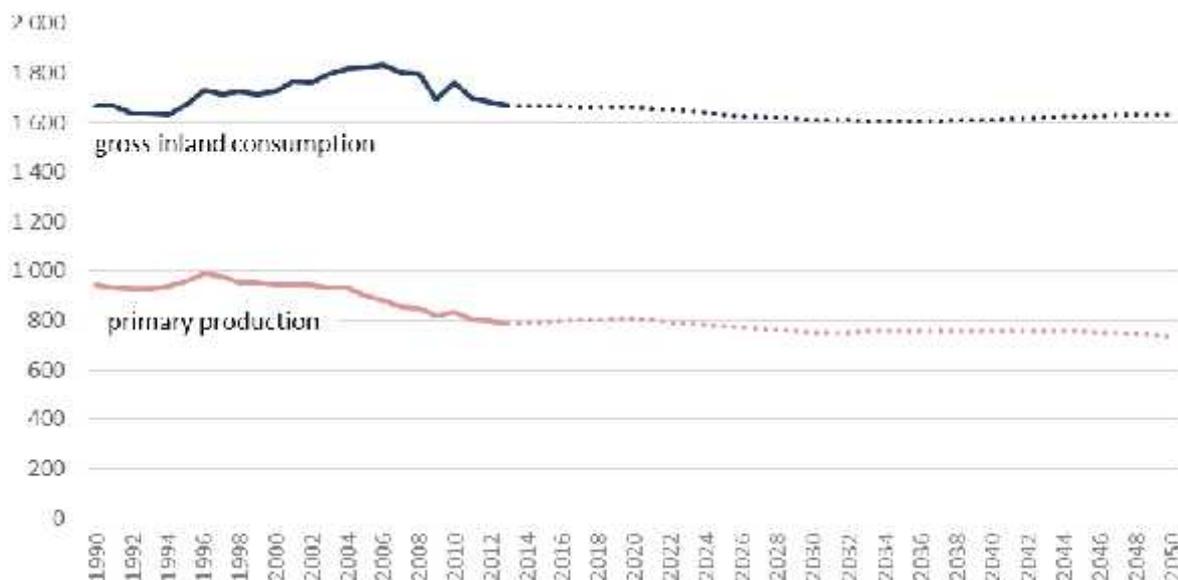
³ Directive 2012/27/EU on energy efficiency.

⁴ Elaboration on Eurostat [nrg_110a]. Unless otherwise stated, this is the source for all figures referring to the current EU energy consumption and production.

⁵ For an assessment of the costs of increasing the share of renewable sources and the timing of a feasible transition, see EC, *Energy Roadmap 2050. Impact assessment accompanying the document*, SEC(2011) 1565/2, part ½, pp. 28-34.

⁶ EC, *EU energy, transport and GHG emissions trends to 2050. Reference scenario 2013*. Unless otherwise stated, this is the source for all figures referring to the future EU energy consumption and production.

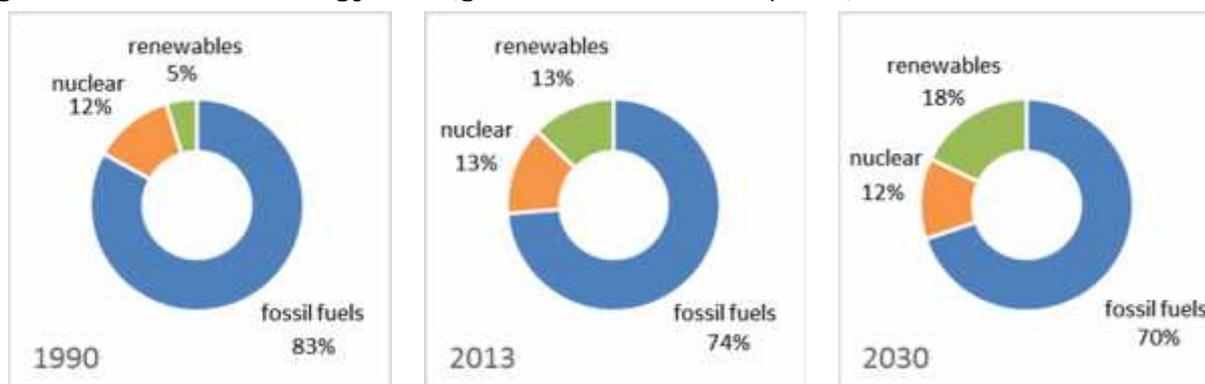
Figure 1 The EU-28 energy gross inland consumption and primary production (Mtoe)



Source: elaboration on Eurostat [nrg_110a] and EC (2013).

Despite a slow, long-term decrease, the supply of fossil fuels is bound to remain at the centre of the European mix (see Figure 2). However, oil, gas and coal have different consumption patterns.

Figure 2 The EU-28 energy mix (gross inland consumption)



Source: elaboration on Eurostat [nrg_110a] and EC (2013).

With 557 Mtoe consumed in 2013, crude oil and refined products consistently represent the first source of energy for Europe due to their unchallenged role in the transport sector (94 %) and, to a lesser extent, in petrochemicals (82 %). However, their consumption is expected to continue a marginally declining trend, from 557 Mtoe in 2013 to 520 Mtoe in 2030, due to improved efficiency in both the final consumption and transformation processes (see Figure 3).

Coal consumption is expected on the contrary to face a steep decline, due to increasing competition from renewable sources and natural gas in the power generation sector. Indeed, coal-fuelled power plants produce high levels of greenhouse gas (GHG) emissions and other pollutants and EU environmental policies are expected to progressively curb coal consumption, from 287 Mtoe in 2013 to 174 Mtoe in 2030.

Natural gas is the only fossil fuel whose consumption is expected to increase in the medium term, due to its comparatively lower level of GHG emissions. Gas demand for power generation, heating buildings and industrial processes is indeed expected to increase from 387 Mtoe in 2013 to 397 Mtoe in 2030.

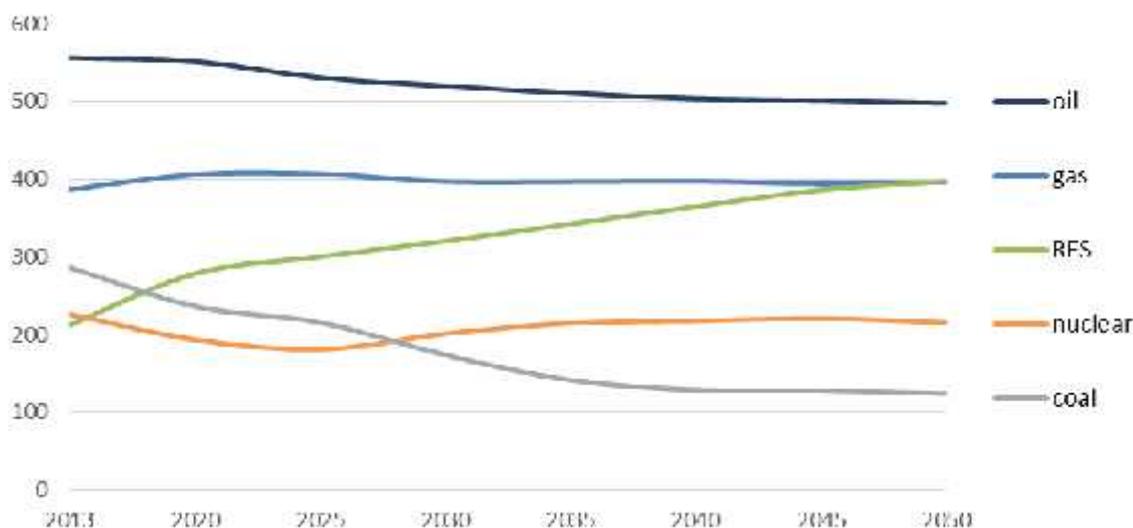
In this context, renewable energy sources represented the most dynamic element of the European energy mix, with consumption growing from 77 Mtoe in 1990 to 212 Mtoe in 2013. This surge in renewables was driven primarily by European energy policies, which set a target of 20% final consumption from renewable sources by 2020⁷. This trend is expected to continue in the coming decades, and in 2030 energy consumption from renewables is expected to reach 320 Mtoe, approximately 20% of the gross inland consumption.

This tendency can be explained by European policies such as massive subsidisation. In 2013, subsidies to renewables amounted to EUR 52 billion and are expected to increase to EUR 60 billion just before 2020⁸. Currently, the EU is the largest financial supporter of renewables in the world, and is expected to hold this position for the coming decades.

This need of financial support is based on the fact that, at the current technological level, the cost of renewable sources is dramatically limiting both the pace of their penetration into the energy mix and their ability to replace fossil fuels as the bulk of European energy consumption.

The other non-carbon source, nuclear power generation, is expected to decrease during the next decade, from 226 Mtoe in 2013 to 181 Mtoe in 2025, before recovering to more than 200 Mtoe after 2030. The most controversial issue with regard to nuclear power is the very high cost of decommissioning, creating a strong incentive to continue operations in existing facilities rather than to close them.

Figure 3 EU-28 expected gross inland consumption, per source (Mtoe)



Source: elaboration on Eurostat (nrg_110a) and EC (2013).

⁷ See the “2009 Climate-energy package”, composed of Regulation (EC) No 443/2009; Directive 2009/28/EC; Directive 2009/29/EC; Directive 2009/30/EC; Directive 2009/31/EC; Decision No 406/2009/EC and setting two binding targets: 20% of energy consumption produced from renewable sources and 20% reduction in greenhouse gas emissions from 1990 levels. Renewable targets are not referring to gross inland consumption, but to final consumption, which does not include transformation losses and consumption by the energy sector.

⁸ International Energy Agency (IEA), *World Energy Outlook 2014*, p. 277-278.

1.1.2 Domestic production and dependence on imported sources

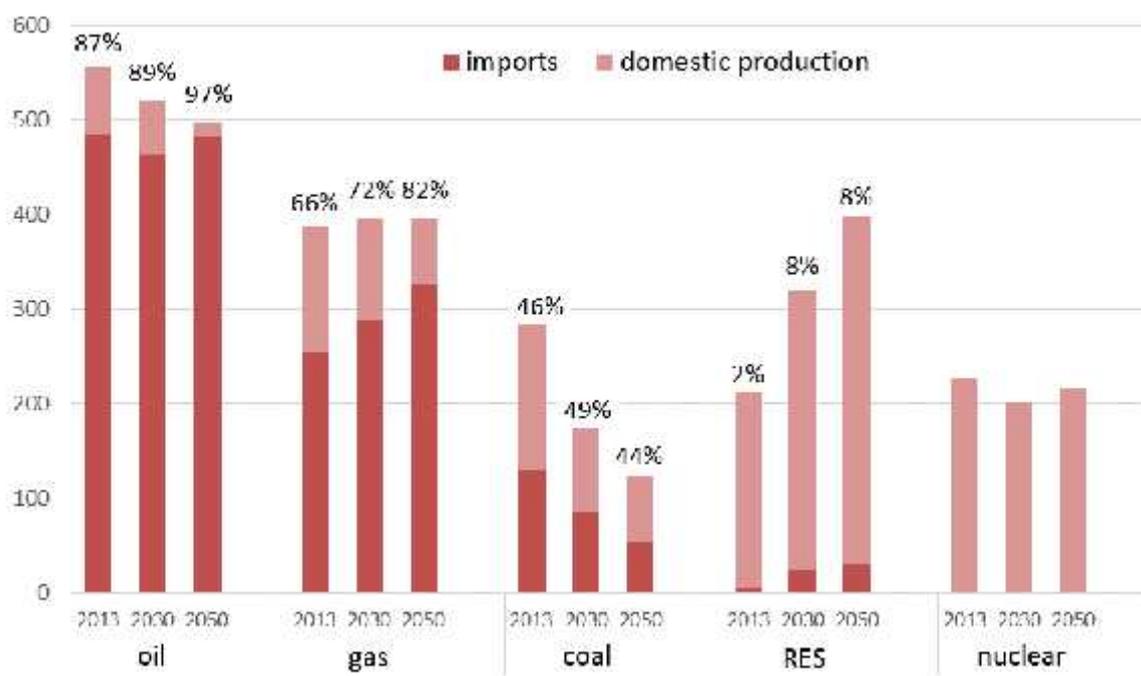
The enduring relevance of fossil fuels in the European energy mix has been coupled with a constant reduction of domestic production since 1995, when it peaked at 958 Mtoe.

The steepest decline occurred in the case of solid fuels: despite large proven reserves still being available, the cost of mining in Europe dramatically increased when compared with international suppliers, pushing more than half of the existing production out of the market. Oil and gas production decreased instead due to the progressive depletion of the existing fields, especially in the North Sea.

Unconventional reserves, such as those of shale gas, are expected to play only a very marginal role in future European production. Indeed, in the EU several factors are hampering a 'shale revolution' similar to the American one: property rights, population density, industry structure, and environmental legislation.

As a result, European energy security increasingly relies on access to international oil and gas markets. This trend is expected to continue in the coming decades and even the long-term increase in renewable sources production is not expected to reverse it (see Figure 4).

Figure 4 Gross inland consumption per source (Mtoe), supply structure and share of imports



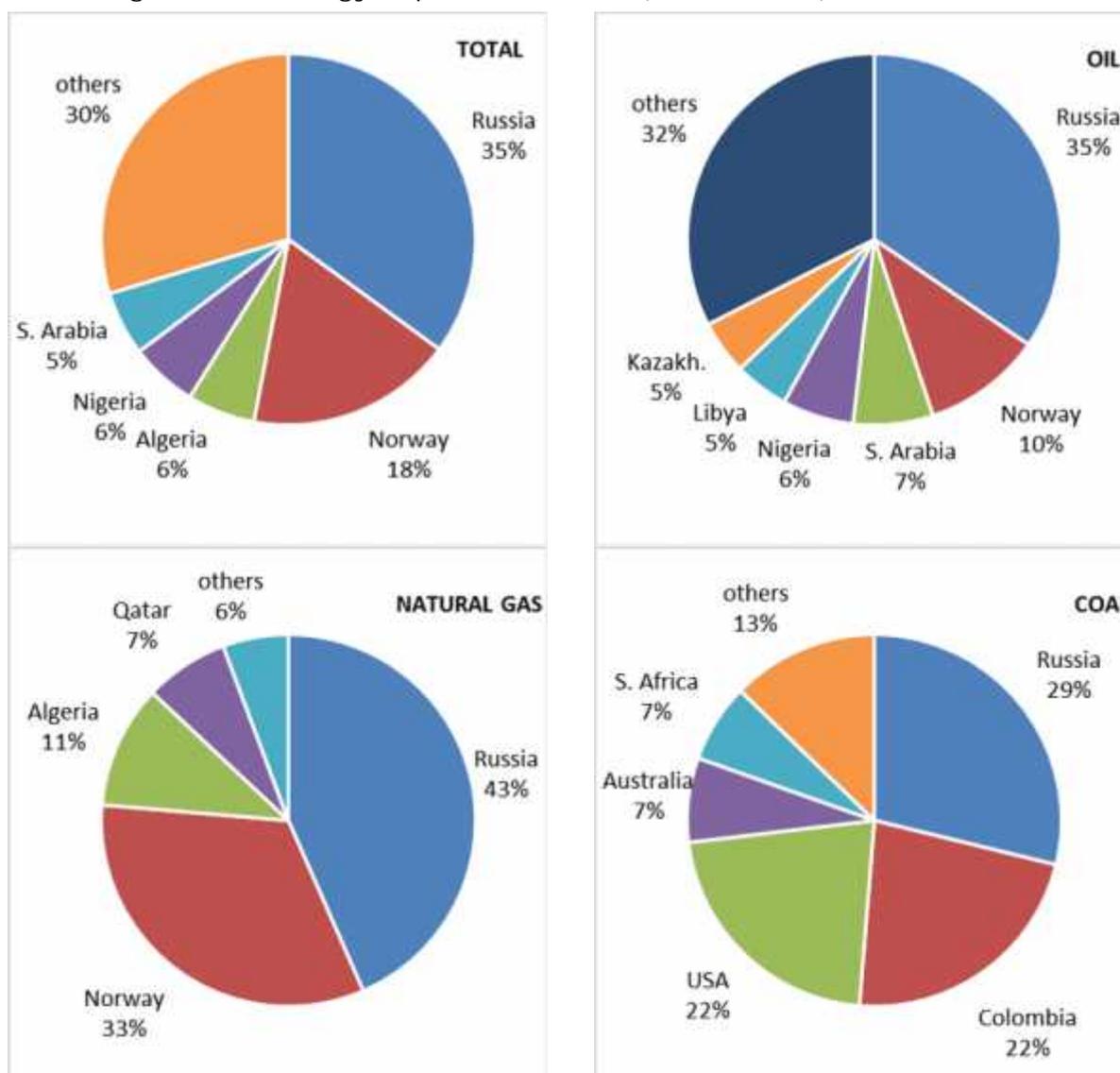
Imports are accounted as non-domestic production.

Source: elaboration on Eurostat [nrg_110a] and EC (2013).

Fossil fuels are traded as commodities on rather heterogeneous markets, with different structures and levels of security⁹. Crude oil and refined products are exchanged on a liquid and substantially global market, where volumes from one exporter can be easily substituted by other sources. Coal is similarly traded on a liquid and global market, with plenty of suppliers exporting by sea.

⁹ For a preliminary assessment of the factors influencing the level of dependence and the structure of the energy supplies, see European Commission Directorate-General for Economic and Financial Affairs, *Member State's Energy Dependence: An Indicator-Based Assessment*, Occasional paper 196, 2014.

Figure 5 Origin of the energy imports of the EU (2013, share)



Source: elaboration on Eurostat [nrg_121a], [nrg_122a], [nrg_123a] and [nrg_124a].

The most challenging issue will be the increasing dependence on imported natural gas. This commodity is traded on a market which, due to the rigidity of gas export infrastructures (i.e. pipelines), is essentially regional. Currently, the European import pipeline system is redundant in terms of capacity – due to the effects of the economic crisis on final demand – and therefore it provides an acceptable level of resilience and security¹⁰. However, the expected increase in imports will require additional infrastructure in order to tap into international markets and meet European final demand, at the same time hedging against the risk of interruption of one of the major supply routes.

The alternative to pipelines, liquefied natural gas (LNG), is only marginally competitive with piped gas in Europe, due to the higher transport costs and the size of the investment needed¹¹. The limited

¹⁰ See ENTSG, *The European Natural Gas Network (Capacities at cross-border points on the primary market)*, June 2014. For a stress test of the European system, see EC, *Communication on the short term resilience of the European gas system*, COM(2014) 654 final.

¹¹ On average, LNG transport is a cheaper option only for distances above 5 000 km, when compared with onshore large-diameter pipelines. Liquefaction-storage-regasification process consumes approximately 15 % of the overall produced gas, compared with approximately 1% in the case of efficient pipelines. Moreover, liquefaction terminals are more complex to build and typically are based on imported technologies. European regional suppliers, which are in the range of a few thousand

competitiveness of current LNG supplies was demonstrated by the sharp reduction in EU LNG imports, which nearly halved between 2011 and 2014, from 70 to 38 Mtoe, despite a total regasification capacity of more than 160 Mtoe per year¹².

The future evolution of LNG supplies to Europe will be influenced by the emergence of a more global market. Indeed, Australia and Papua New Guinea are adding new export capacity, while new plants will be commissioned in South-East Asia and North America, oversupplying regional markets and creating the conditions for a stronger integration at the global level¹³. At the same time, the global tanker fleet is increasing in number and capacity. However, LNG prices on East Asia markets are substantially higher than prices in Europe and European operators have to compete with them in order to import larger volumes¹⁴. The actual impact of increased LNG supplies at the global level on the European gas markets will largely depend on the size of this differential: if a full-scale convergence takes place, LNG supplies will recover well above 2011 levels. However, for this decade the Europe-Asia LNG price differential is expected to remain significant, limiting the likely recovery of LNG imports to 2011 levels.

Either piped or liquefied, natural gas is expected to play a major role in the process of decarbonisation of the European economy, while at the same time preserving its competitiveness. However, the lack of a truly global market and the enduring relevance of import pipelines will require a strong political involvement to underpin and secure trade relations at the regional level. The situation is particularly complex since a large share of European consumption is coming from the former Soviet Union (25 %) and from North Africa (10 %)¹⁵. A particular challenge will come from transit countries, where political stability and reliability of gas flows may be endangered, such as Ukraine, Tunisia and Turkey, which respectively carry gas from Russia, Algeria and Central Asia.

Beside fossil fuels, renewables are also increasingly being imported, despite their small incidence¹⁶. In 2013, imported biomasses, biofuels and wastes accounted for 5 Mtoe (out of 212 of RES consumption) and are expected to increase up to 25 Mtoe in 2030 (out of 320). A low level when compared with fossil fuels, but rapidly increasing in terms of value, especially in the case of biofuels.

1.1.3 Value of energy trade

Energy imports represent a major element of EU trade. In 2013, fossil fuel imports amounted to EUR 492 billion, 29 % of all European imports. Crude oil and refined products represented the largest share (EUR 390 billion), with natural gas (EUR 86 billion) and coal (EUR 17 billion) accounting for the rest (see Figure 6).

kilometres, are therefore expected to continue to resort largely to pipelines and enjoy lower transport costs than long-distance LNG supplies. The scope of this advantage depends on the distance and the actual location of the suppliers, being higher for those exporters who have to rely on canals (such as Suez) or who cannot use very large vessels (such as Q-Max carriers). See D. Bonhomme et al, *Competition: pipeline gas and LNG in Europe*, paper presented at the LNG 17 Conference Session, Gas Technology Institute, 2013; G. Pireddu, *Economia dell'energia - I fondamenti*, second edition, CLU, 2015, pp. 213-214; and B. Songhurst, *LNG Plant Cost Escalation*, NG83, Oxford Institute for Energy Studies, 2014.

¹² JODI, *Gas World Database*.

¹³ See Groupe International des Importateurs de Gaz Naturel Liquéfié, *The LNG industry in 2013*, 2014.

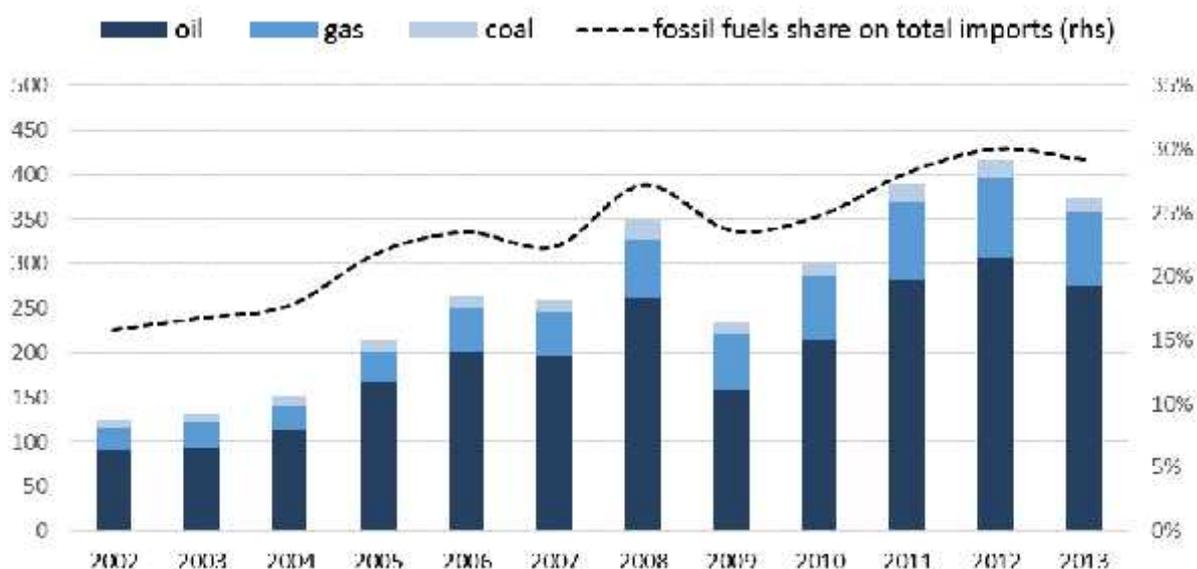
¹⁴ For instance, during the last three years, LNG import prices in Japan (the leading market in Asia) have been consistently higher than import prices of piped gas in Germany (the leading market in Europe), with a differential between +15 % and +70 % on average. However, in the East Asian LNG market, oil indexation is stronger and lower oil prices could entail a lower differential. See European Commission (EC) – DG Energy, *Quarterly Report Energy on European Gas Markets*, Market Observatory for Energy, 7(3), 2014.

¹⁵ Eurogas, *Statistical Report 2014*.

¹⁶ The actual source of more than three quarters of extra-EU liquid biofuels imports is 'Not specified', as reported by Eurostat [nrg_126a]. In 2013, the largest suppliers were Indonesia (15%) and Switzerland (2%),

The European oil refining sector is also a world-class industry, competing at the global level with a capacity of 16.8 million barrels per day, i.e. 18 % of the world total¹⁷. In 2013 refined products exports amounted to EUR 115 billion, 7 % of EU total exports. Even if the value of the exported volumes is inevitably influenced by the oil prices, which halved in 2014, the European refining industry remains a relevant part of the sector at the global level. As regards to other sources, the EU re-exported EUR 4 billion of gas and EUR 1 billion of coal.

Figure 6 EU-28 net imports of oil, gas and coal (in billion euros) and share of fossil fuels on total imports



Source: elaboration on Eurostat [DS-018995].

EU fossil fuel imports are projected to reach around €500 billion in 2030 and €600 billion in 2050, in constant 2010 euros. In fact, independent of fluctuations in oil prices, energy imports are expected to represent a major element of the European trade balance¹⁸.

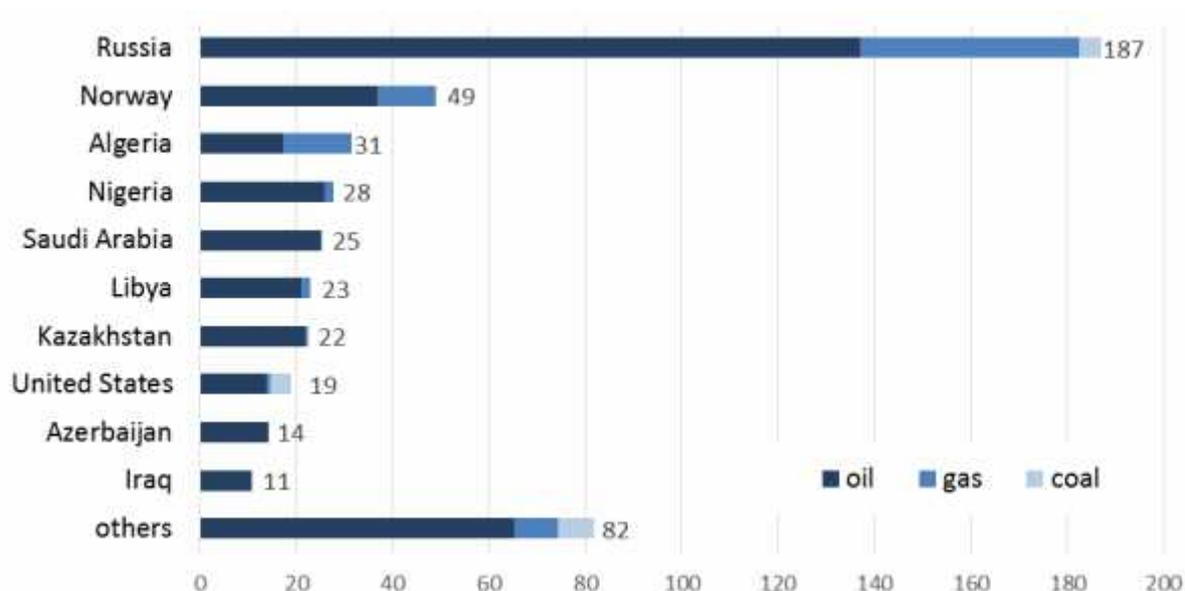
1.1.4 Main trading partners

The most important suppliers of fossil fuels to the EU are Russia, Norway and Algeria (see Figure 7). Crude and oil products represent the most important commodities, but natural gas represents a major item in all three cases.

¹⁷ IEA, *World Energy Outlook 2014*, p. 132.

¹⁸ EC, *EU energy, transport and GHG emissions trends to 2050. Reference scenario 2013*, p. 50.

Figure 7 Top-10 EU-28 energy suppliers (2013, euros)



Russian figure includes category "countries and territories not specified for commercial or military reasons in the framework of trade with third countries".

Source: elaboration on Eurostat [DS-018995].

1.1.5 The Energy security strategy and expected evolutions

The EU energy and environmental policies are aiming at a transition to a low-carbon economy, which is expected to reduce the use of imported fossil fuels, by moderating energy demand and by exploiting renewable and other indigenous resources.

In particular, *A policy framework for climate and energy in the period from 2020 to 2030* paved the way for new, ambitious targets: 27% of final energy consumption from renewables and 40% of GHG emissions reduction from 1990 levels¹⁹. In October 2014, the European Council endorsed these targets, providing sound political support for the proposals of the European Commission notwithstanding different national approaches to the issue of climate change. Despite their ambition, these targets are not expected to reverse the current trend of growing dependence, since energy imports remain too important for the competitiveness of the European economy.

The *Energy security strategy*, adopted in June 2014, is focused on interconnections and internal market completion, which would indeed enhance resilience but which cannot reverse European dependence on imported fuels²⁰. Also the *Energy Union package*, adopted in February 2015, is intended to foster more intervention at European and national level in order to achieve a fully integrated market. However its effectiveness in reducing import dependence and market fragmentation will largely depend on future political action and cannot be currently assessed²¹.

Overall, energy trade is likely to remain the most important source of energy supplies for the European economy. Consequently, access to liquid, diversified and reliable international markets is expected to remain the single most important element of the European energy security strategy.

¹⁹ EC, *A policy framework for climate and energy in the period from 2020 to 2030*, COM(2014) 15 final.

²⁰ EC, *European Energy Security Strategy*, COM(2014) 330 final.

²¹ EC, *Energy Union package. A Framework Strategy for a Resilient Energy Union with a Forward-Looking Climate Change Policy*, COM(2015) 80 final.

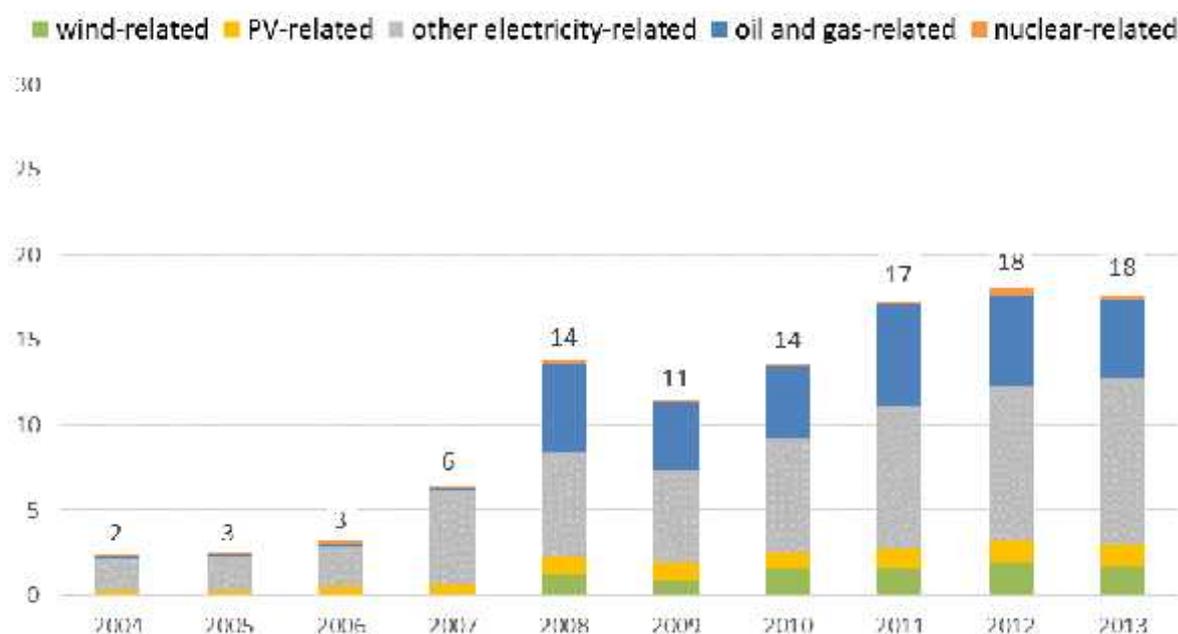
1.2 Industrial interests

The energy sector is also important from an industrial perspective. EU companies are significant manufacturers of machinery and industrial goods related to all main energy sources and technologies, as well as providers of services and foreign direct investments (FDI)²².

1.2.1 Exports and imports of energy-related goods and services

European exports of energy-related goods grew significantly during the past decade, from EUR 2 billion in 2004 to EUR 18 billion in 2013. Electricity, wind and oil and gas were the most relevant sectors (see Figure 8).

Figure 8 EU-28 exports of energy-related goods (billion euros)



Source: elaboration on Eurostat [DS-056120].

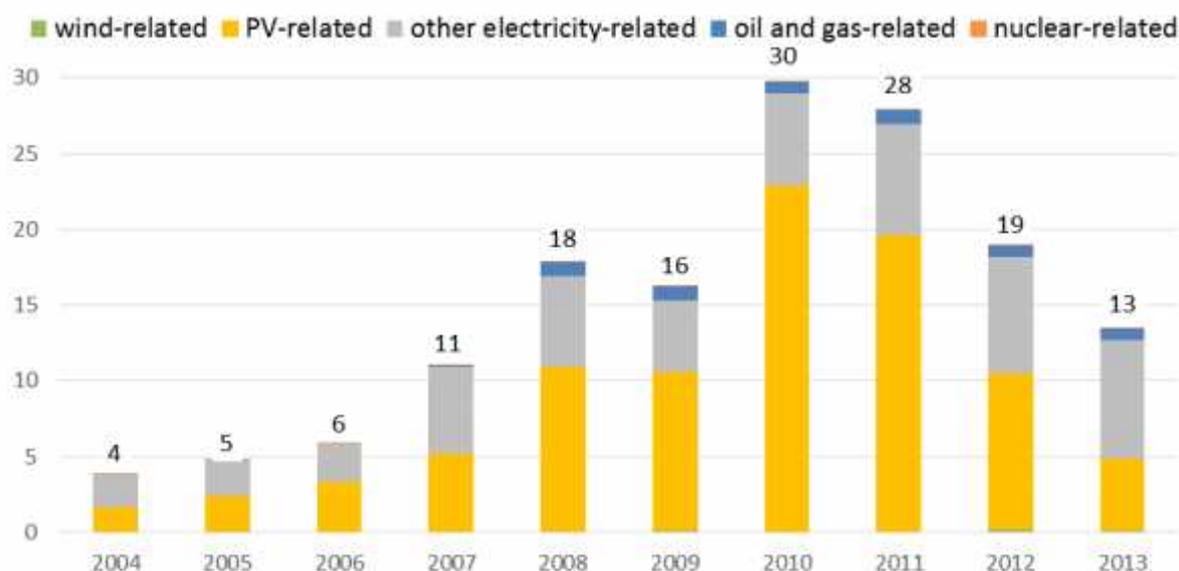
European economies are also large importers of energy-related goods, and ran a consistent trade deficit until 2012. The main driver of this trend was a surge in imports of photovoltaic (PV) panels, due to large subsidisation plans. Indeed, cumulated imports of PV panels during the past decade amounted to EUR 83 billion, with a peak of EUR 23 billion in 2010 (see Figure 9). In 2013, a reduction in new subsidies lowered imports of PV panels to EUR 5 billion, as the EU became a net exporter of energy-related goods.

European companies also export energy-related services. In particular, in 2013 pipeline transport services' exports amounted to EUR 1.4 billion, while sale of services related to electricity transmission amounted to EUR 200 million²³.

²² European FDI in energy-related sectors are not detailed in this report because official figures are not available on Eurostat. See *EU direct investment flows, breakdown by partner country and economic activity (BPM6) [bop_fdi6_flow]* - Last update: 06-02-2015.

²³ Eurostat, *International trade in services (since 2010) (BPM6) [bop_its6_det]*. Other services are instead more difficult to estimate, since their figures are reported aggregated with non-energy services, as in the case of 'Engineering services'.

Figure 9 EU-28 imports of energy-related goods (billion euros)



Source: elaboration on Eurostat [DS-056120].

The amount of EU investment in third countries is in contrast particularly difficult to assess and quantify. Indeed, European and international statistics referring to the foreign direct investment in energy-related sectors are partial, since they are usually reported mixed with non-energy sectors (as in the case of petrochemicals, or machinery). Moreover, extra-EU investment made by EU-based companies are difficult to define and account for, since they are often carried out by controlled societies (companies?) which are not included in EU statistics.

Nonetheless, most recent available figures are useful to outline the relevance of the international projection of the European companies. In 2011, EU direct investment positions in the extraction of hydrocarbons outside the EU amounted to EUR 368 billion, while manufacture of petroleum, plastic products and coke amounted to EUR 568 billion and electricity and gas supply amounted to EUR 64 billion²⁴.

EU-based international oil companies are also involved in several large-scale projects, devoted to supply European markets. For instance, BP is the largest shareholder in the Shah Deniz Stage 2 and South Caucasus Pipeline (SCP) expansion projects, which will represent the first actual project of the Southern Gas Corridor and will cost approximately EUR 24.8 billion over one decade²⁵. In contrast, Eni capital expenditure in North Africa – a key area for oil and gas supplies to Europe – exceeds EUR 1 billion per year²⁶.

The value of EU-based companies' participation in energy-related procurement in third countries cannot be confidently assessed. EU countries are indeed parties of the Government Procurement Agreement (GPA) in the World Trade Organization²⁷, but there is no updated statistics available on the size of the activities of EU-based companies in third countries with specific reference to public procurement.

²⁴ EU-27. Eurostat, *EU direct investment positions, breakdown by country and economic activity (NACE Rev. 2) [bop_fdi_pos_r2]*.

²⁵ See BP Caspian Website, www.bp.com/en_az/caspian/operationsprojects/Shahdeniz/FAQ.html.

²⁶ Eni, *2014 Fourth Quarter and Full Year Preliminary Results*, 28 February 2015.

²⁷ See Chapter 3.1.

2 Energy policy and trade policy

The EU relies heavily on energy imports from other countries and this makes access to open, transparent and stable international energy markets particularly important. However, international trade in energy is quite different from that in other goods or services because it is an essential input for every economic activity. And, in many cases, it is difficult to stock it in quantities large enough to cover a long period of consumption. Restrictions on its availability, both in terms of quantity and price, have a profound negative impact on households and firms. Therefore, a proper energy policy should devote considerable attention to the issue of security of supply, something that is generally less relevant to trade policies.

Today the EU has a competence both in energy and trade, however the decision-making process and the development of a European policy in these areas differs in many respects. Indeed, while trade is an exclusive and well established competence of the EU, energy received a formal inclusion among the competencies shared by the EU and Member States only with the Lisbon Treaty in 2009. As a consequence, national governments still have strong competences in energy matters and remain in charge of providing security to their citizens and firms. Nevertheless, critical situations like the Russian-Ukrainian crisis call for new and more significant initiatives at the Union level, especially as far as security of supply is concerned.

In the following sections a description of the fundamental elements of EU energy law and policy will be provided, together with a comparison with EU trade policy and the particular case of the Raw Material Initiative. Following this, the current proposal for an Energy Union will be considered. Finally, a list of the ways in which trade provisions impact on the energy sector will be presented.

2.1 EU energy law and policy

Energy policy is today an important issue in European affairs but this has not always been the case. From the 1960s to the 1990s, energy policy was essentially decided at the national level and only the Lisbon Treaty formally recognised a shared competence for the EU, a development which confirmed the legality of the role acquired by EU institutions in the previous two decades.

2.1.1 The establishment of the EU competence on energy

Energy was one of the policy areas that was at the centre of European integration in the very beginning. When the Treaty of Paris on the European Coal and Steel Community was signed in 1951, coal represented the most important energy source for European economies. Nuclear energy was considered to be the energy of the future when in 1957 Belgium, France, Germany, Italy, Luxemburg and the Netherlands signed the Treaty of Rome on the European Atomic Energy Community.

However, after such a bright start, energy policy was progressively side lined and Member States preferred to maintain strong control over the matter. This was due to the importance of energy for national security, wide differences in the endowment of energy resources and consumption patterns, the existence of large and often monopolistic state-owned energy companies and the possibility to use energy policy for implementing social and industrial policies at the domestic level.

The attitude began to change in the late 1980s and early 1990s, when the Single European Act revived the goal of completing the Internal Market. The Gulf War and the dissolution of the Soviet Union again brought attention to the issue of security of supply and, finally, growing concerns about climate change called for a more sustainable energy sector. Since then, the European Commission – joined later by the European Parliament – has been working hard to establish a role for the EU institutions, along with a proper European energy policy. In the absence of an explicit acknowledgment of such a competence in the Treaties, the Commission resorted to the provisions on internal market, competition, trans-European networks and environmental policies scattered here and there within EU primary law as the legal basis for its own initiatives.

Although priorities have changed over time, the main objectives of the European energy policy developed since the beginning of the 1990s have remained essentially the same: competitiveness, security of supply and sustainability. They form the ‘energy triangle’, within which the policy initiatives undertaken in the last 20 years could be grouped (liberalisation of the electricity and gas markets, unbundling of networks, development of interconnections, promotion of renewable sources, energy efficiency of products and buildings, diversification of supply routes and countries, reduction of greenhouse gas emissions, etc.).

The pursuit of these three goals has not been easy and tensions have frequently surfaced due to several trade-offs, for instance between competitiveness and sustainability or between competitiveness and security of supply. This has happened despite the Commission repeatedly underlining how such objectives are compatible and could be pursued more efficiently together, through coherent and comprehensive policies²⁸.

2.1.2 The provisions of the Lisbon Treaty

The Lisbon Treaty formally recognised the policy developments that had occurred since the early 1990s. Article 4 of the Treaty on the Functioning of the European Union (TFEU) provided for ‘shared competence between the Union and the Member States [...] in the areas [of] trans-European networks [and] energy.’

Title XXI of Part Three of the TFEU specifies the content of such shared competence over energy²⁹. Article 194, the only one of title XXI, states explicitly in the first paragraph the four objectives that the Union’s policy on energy shall aim towards:

- ensuring the functioning of the energy market;
- ensuring security of supply in the Union;
- promoting energy efficiency and energy saving and the development of new and renewable forms of energy; and
- promoting the interconnections of energy networks³⁰.

These objectives, that are coherent with the three main goals of competitiveness, security and sustainability have emerged, de facto, since the 1990s, must be pursued ‘in the context of the establishment and functioning of the internal market and with regard for the need to preserve and improve the environment [...] in a spirit of solidarity between Member States’. Therefore, European energy policy must resort extensively to competitive markets and take in due consideration its environmental impact, as well as the needs of the weakest Member States or of those that have been affected by natural or man-made disasters, or by terrorist attacks³¹.

The autonomy of national governments over energy has nevertheless been partially preserved by the Lisbon Treaty. Indeed, paragraph two of Article 194 reaffirms the traditional principle that the measures adopted by the Union ‘shall not affect a Member State’s right to determine the conditions for exploiting its energy resources, its choice between energy sources and the general structure of its energy supply’. On these issues the EU can adopt a decision, in order to pursue its environmental goals, only through a special

²⁸ One of the official documents that expresses clearly this view of the European Commission is the Green Paper on A European Strategy for Sustainable, Competitive and Secure Energy, COM(2006) 105.

²⁹ Part Three of the TFEU is devoted to Union policies and internal actions.

³⁰ Articles 170-172 TFEU are specifically dedicated to trans-European networks in the areas of transport, telecommunications and energy.

³¹ The spirit of solidarity is explicitly referred to energy issues also in Article 122 TFEU, where it is stated that: ‘the Council, on a proposal from the Commission, may decide, in a spirit of solidarity between Member States, upon the measures appropriate to the economic situation, in particular if severe difficulties arise in the supply of certain products, notably in the area of energy.’ However, it should be noted that the verb used here is ‘may’ and not ‘must’.

legislative procedure, with the Council agreeing by unanimity after having consulted the European Parliament, the Economic and Social Committee and the Committee of the Regions (Article 192(2)).

Unanimity in the Council and consultation of the European Parliament are required also for establishing measures that are primarily of a fiscal nature (Article 194(3)). In all other cases decisions must be taken by the European Parliament and the Council in accordance with the ordinary legislative procedure – formerly known as the co-decision procedure – after having consulted the Economic and Social Committee and the Committee of the Regions (Article 194(2)).

In conclusion, despite the said provisions of the Lisbon Treaty, the competence of the EU in energy matters is quite limited and in many aspects weaker than in federations like the United States of America or Canada. For example, in these countries ‘fossil fuel reserves are property of the states, provinces or private landowners, but federal authorities usually have the power to define depletion policies, levy royalties, impose retail taxes and own all off-shore and some on-shore reserves’³². While to some extent this weakness is counterbalanced internally by the legal authority of the Commission over the single market, competition and state aid issues, the external aspects of the European energy policy are still today particularly underdeveloped – the reference in Article 194 to ensure security of supply is not especially extensive – and Europe usually does not speak with a single voice.

2.2 A comparison with EU trade policy

Since the establishment of the European Economic Community (EEC) in 1957, trade policy has been an exclusive competence of the European institutions. This was necessary in order to properly manage the custom union and preserve the integrity of the internal market. Over time, the Commission has promoted a free trade approach in international forums and has acquired significant expertise by representing the interests of the Union as a whole in trade negotiations at the bilateral, interregional and multilateral level. Recently, the Treaty of Lisbon confirmed the supremacy of EU institutions over trade-related issues such as intellectual property rights and public procurement, which have become increasingly important in the current globalised and dematerialised world economy³³.

2.2.1 The EU exclusive competence in trade policy

Whilst European national governments still enjoy significant autonomy in energy policy, in trade policy the EU actually speaks with one voice to its commercial partners and the rest of the world. Since the establishment of the EEC the Union has a Common Commercial Policy (CCP), which aims – according to the new formulation after the Lisbon Treaty – at contributing to the ‘harmonious development of world trade, the progressive abolition of restrictions on international trade and on foreign direct investment, and the lowering of customs and other barriers’ (Article 206)³⁴.

Article 207 TFEU gives the European Parliament and the Council the right to define the framework of the CCP, also following proposals by the Commission. The latter is then responsible for the implementation of the framework, both through ‘trade promotion’, i.e. the negotiation and signature of agreements at bilateral, interregional and multilateral levels, and through ‘trade defence’, i.e. the implementation of reactions and countermeasures to perceived unfair trade practices by commercial partners.

In implementing the CCP, the EU tries to balance the interests of the Member States and of the different stakeholders (consumers, producers, importers, exporters, environmentalists, workers, human right activists, etc.). This is done with a view to ensuring fair competitive conditions for European companies;

³² D. Buchan, *Energy and Climate Change: Europe at the Cross Roads*, Oxford University Press, Oxford, 2009, p. 9.

³³ Services and ideas are becoming today more important than goods.

³⁴ Articles 206 and 207 on the CCP form Title II of Part Five of the TFEU, which is devoted to the Union’s external action.

allowing the import of raw materials and other productive inputs into Europe; making available more goods and services to European consumers; fostering growth, innovation and employment and, eventually, helping the least developed countries by unilaterally granting open access to the EU internal market.

There are several tools available for implementing the CCP. Traditionally tariffs, quotas and subsidies were the most important instruments of trade policy, but in recent years a more relevant role has been acquired by non-tariff or technical barriers to trade, like custom practices, standards for plant and animal health, rules on product safety, licensing procedures, limits to public procurement, intellectual property rights (IPRs), domestic taxes, profit repatriation and legal protection for FDIs. This evolution, recognised by the new wording of Article 207 TFEU, is due to the profound changes that have occurred in international trade patterns, such as the emergence of multinational companies, a stronger international division of labour, the establishment of long and complex supply chains, and the increased importance of ideas and services vis-à-vis goods and commodities.

2.2.2 The Raw Materials Initiative

Although in recent decades trade in manufactured goods, services and other trade-related issues such as IPRs or FDI have become more important in the CCP, trade in raw materials still has considerable relevance for the EU. This is the case especially because Europe has inadequate domestic endowment of metals (platinum, cobalt, magnesium, etc.), fossil fuels (oil, natural gas and coal), non-metallic minerals (graphite) and some biological feedstock (wood, natural rubber, etc.), which are often indispensable inputs to the European manufacturing sector. Indeed, the competitiveness of EU industry requires efficient and secure access to raw materials, something that should not be taken for granted because of the significant increase in world demand and the extreme volatility of prices recorded in markets that are often not transparent nor liquid.

In this context of dependency, the European Commission launched in 2008 the Raw Materials Initiative (RMI), an integrated strategy in response to the different challenges related to access to non-energy and non-agricultural raw materials³⁵. Its aim is to guarantee unhindered access for European firms to raw materials and cope with potential shortages due to a highly concentrated supply, political and economic instability or restrictive policies in producing countries, international competition, a low level of substitutability and inadequate recycling.

The RMI is based on three pillars:

- ensuring a level playing field in access to resources in third countries;
- fostering sustainable supply of raw materials from European sources;
- boosting resource efficiency and promoting recycling, thereby reducing import needs³⁶.

Central to this strategy is a 'raw material diplomacy', anchored in a wider approach towards third countries (regional stability, conflict resolution, good governance, human rights promotion, etc.) and aimed at pressing for the elimination of restrictions on export (bans, quotas, exporting duties and licensing) or limits to FDI by European firms in the mining sector. This point is particularly relevant because, in the Commission's own words, 'securing supplies of raw materials is essentially the task of companies and the

³⁵ European Commission, *The raw material initiative – meeting our critical needs for growth and jobs in Europe*, COM (2008) 699. An update of such initiative could be found in European Commission, *Tackling the challenges in commodity markets and on raw materials*, COM(2011) 25.

³⁶ The RMI is part of one of the flagship initiatives under the Europe 2020 Strategy, that for a resource-efficient Europe.

role of public authorities is to ensure the right framework conditions to allow companies to carry out this task', i.e. to have open and undistorted access to natural resources in foreign countries³⁷.

The annual reports of the Commission suggest the Initiative has generated good results³⁸. As far as the first pillar is concerned – the one of more relevance in this study – in recent years the Commission has been able to put the issue of open and fair access to raw materials high on the international agenda and to obtain clear and binding commitments by countries that are joining the WTO or with which it is negotiating trade agreements. Moreover, the EU has successfully filed lawsuits at the WTO level against countries that had put in place policies hindering international trade in raw materials³⁹. The transparency and knowledge of worldwide raw materials supply chains have also been increased.

In some cases, protectionist economic policies of resource-rich countries are limiting the efforts of the Commission, but the decline in commodity prices and the economic slowdown since the beginning of 2014 have somewhat eased these problems and made the issue of access to raw materials less contentious.

2.3 The Energy Union: a new idea or just a cosmetic make-up?

The RMI could be a good example of a European policy, justified by a common condition of dependency on imports and based on collective actions. However, as explained above, collective actions over energy have been difficult to agree upon and implement. Indeed, only in situations of crisis – like the gas conflicts between Ukraine and Russia – has the security dimension of energy attracted the attention of policy makers, leading to discussions and possibly the adoption of concrete policy initiatives⁴⁰.

2.3.1 The Tusk proposal

This policy pattern was evident in 2014 as well. After the deepening of the Ukrainian crisis and the annexation of Crimea by the Russian Federation, concerns over the reliability of Russian energy supplies and dissatisfaction with the possibility for Moscow to blackmail European countries over foreign policy issues grew large, especially among Eastern European Member States⁴¹. In this context, the then Prime Minister of Poland, Donald Tusk, formulated the idea of building an Energy Union. In an article published in the *Financial Times* in April 2014, he called for the establishment of a 'single European body charged with buying Russian gas', which would allow European countries to coordinate their economic transactions with Gazprom, the Russian quasi monopolist for gas export, and reduce its market power⁴².

According to Mr Tusk, who has now become the President of the European Council, the Energy Union should be built having in mind the example of the Euratom Supply Agency and it should be based on solidarity and common economic interests. Bilateral energy agreements should be stripped of any secret and market distorting clauses; a template contract should be created for all new gas contracts and the European Commission should be required to take a role in all new negotiations. Together with this coordinating mechanism, the Energy Union would have five other pillars: a solidarity mechanism for helping countries hit by supply disruptions (coordinated emergency measures and pooled gas storage facilities); an adequate and interconnected European energy infrastructure co-financed by the EU; a larger

³⁷ European Commission, *Tackling the challenges*, COM(2011) 25, p. 14.

³⁸ European Commission, *On the implementation of the Raw Materials Initiative*, SWD(2014) 171.

³⁹ A good example is the lawsuit against China and its policy of export duties and other restrictions to the export of rare earths.

⁴⁰ D. Buchan, *Energy Policy: Sharp Challenges and Rising Ambitions*, in Wallace H., M. Pollack and A. Young (ed.), *Policy Making in the European Union*, Oxford University Press, Oxford, 2010, p. 370.

⁴¹ Eastern European Member States are usually more concerned about Russia due to their relatively larger dependency on Russian energy supplies, the more limited availability of alternative energy supplies and the memory of the Soviet domination in the 20th Century.

⁴² D. Tusk, *A united Europe can end Russia's energy stranglehold*, *Financial Times*, 21 April 2014.

exploitation of domestic fossil fuel reserves; a better engagement with energy partners outside Europe; and a strengthened Energy Community that involves Eastern neighbouring countries.

The proposal of Mr Tusk, with its hint at a common control over resources and a common purchase of gas, was probably too emphatic but it contributed to the debate on a European energy security strategy that culminated with a communication by the Commission in May 2014 and the conclusion of the European Council in June 2014⁴³. Indeed, in these two documents several of the elements that form the basis of the Energy Union according to Mr Tusk were listed, but lukewarm reference was made to the possibility of aggregating gas demand and purchase gas collectively⁴⁴.

2.3.2 Recent developments and a limited political endorsement

A few weeks after the meeting of the European Council, the then candidate for President of the Commission, Jean-Claude Juncker, revived interest in the concept by making the realisation of an Energy Union one of the priorities of his term in office. Mr Juncker, who subsequently got the green light for his position by the European Council and the European Parliament, underlined the necessity to reform and reorganise the European energy policy into an Energy Union, where Member States pool their resources, combine their infrastructure, unite their negotiating power vis-à-vis third countries, diversify their energy sources and reduce their dependency on imports. Mr Juncker acknowledged his commitment to free trade and open access to the internal market for EU's neighbours, but remarked that 'if prices were to become too expensive in commercial or in political terms, the EU should be able to switch very swiftly to other supply channels'. In order to do that the EU should, according to Mr Juncker, be able to reverse energy flows, increase the share of renewables in the energy mix and enhance energy efficiency⁴⁵.

This vision has been apparently shared by Maroš Šefčovič, the new Vice President for the Energy Union, and Miguel Arias Cañete, the new Commissioner for Climate Action and Energy. The former, in particular, has repeatedly expressed in public his idea of an Energy Union based on five pillars. The first of such pillars is centered on a more assertive energy diplomacy, coherent with the economic relevance of the European internal market; on a larger cooperation and consultation between Member States over gas purchasing contracts, possibly developed step by step; and on the opening of the Southern gas corridor for non-Russian gas⁴⁶.

After much fanfare, at the end of last February the Commission produced a Communication on the topic. However, no new element was added by the Communication, which instead restated the traditional priorities and policies of the EU, this time with a clear stress on security of supply and affordability for consumers⁴⁷. Indeed, the most innovative elements that had been discussed in the previous months, like the single gas buyer, were somehow downgraded.

The conclusions of the March 2015 European Council go further in this direction: the Heads of State and Government expressed their commitment to the idea of the Energy Union but put more emphasis on the development of cross-border infrastructures, the implementation and enforcement of existing legislation, a

⁴³ European Commission, *European Energy Security Strategy*, COM(2014) 330.

⁴⁴ In the Conclusions to the European Council there was no mention to the single buyer proposal, whereas the Commission expressed in the May communication its intention to examine procedures that would increase the transparency of international gas markets and their ability to take into account energy security needs. In addition to that, it expressed its availability to assess demand aggregation mechanisms, especially in order to ensure compatibility with EU legislation and trade law. European Commission, *European Energy Security Strategy*, p. 19.

⁴⁵ J.-C. Juncker, *A new Start for Europe: My Agenda for Jobs, Growth, Fairness and Democratic Change*, Opening Statement to the European Parliament, Strasbourg, 15 July 2014, pp. 5-6.

⁴⁶ The other four pillars envisaged by Mr Šefčovič are the internal energy market, energy efficiency, decarbonisation of the energy mix and more R&D in energy technologies.

⁴⁷ European Commission, *Energy Union Package*, COM (2015) 80.

well-functioning internal market, the increased reliance on domestic resources and on energy efficiency. In the words of the European Council, there is no reference to pre-emptive control by the Commission of intergovernmental agreements related to the purchase of energy from third countries: transparency and compliance with existing legislation is necessary, but the confidentiality of commercially sensitive information needs to be guaranteed as well. The use of all external policy instruments to establish strategic partnerships with producing and transit countries is accepted but the idea of a single gas buyer has been turned into a mere 'voluntary demand aggregation mechanism', whose compliance with EU and WTO rules must however be assessed in the coming months⁴⁸.

2.4 Impacts of trade policies on the energy sector

Notwithstanding the eventual evolution of the proposal for an Energy Union and the establishment of a single gas buyer, EU trade policies already have a strong impact on the energy sector today. Indeed, trade agreements are very important in defining the development of international energy markets and the possibility for countries dependent on imports to ensure enough supplies. Without any intention to be exhaustive, it is possible to list some examples of how trade policies affect flows of energy or energy-related capital goods:

- bans on the export of energy sources, as in the case of the ban on crude oil exports enacted by the US Congress since 1975: given the limited capacity of US refineries, the ban is one of the main culprits for the growing gap between the Brent crude and the West Texas Intermediate prices;
- granting of a monopolistic right to export to a company of the producing country, as in the case of Gazprom, which enjoys the exclusive right to export natural gas out of Russia via pipelines: given the low profitability of the Russian domestic gas market and the high costs to export gas via LNG, foreign companies have little incentive to invest in the Russian gas upstream sector;
- introduction of a duty on export of energy sources;
- prohibition of foreign firms to invest in the mining or in the energy sector;
- lack of legal protection for foreign investors;
- minimum national content for public procurement, as in the case of Brazil, which has implemented strict conditions for the exploitation of *pré-sal* oilfields that limit the participation of foreign oil service companies and hinder the export potential of capital goods from other countries;
- discrimination in the taxation of revenues for domestic and foreign firms.

Rules concerning these and many other aspects change from case to case depending on the trade agreement existing between the EU and the respective foreign country. Indeed, as the next sections will illustrate, the EU has agreed on numerous different trade agreements in recent decades, ranging from the basic conditions implied by the accession to the World Trade Organisation (WTO), to deeper agreements signed with accession countries like Turkey or Serbia.

⁴⁸ The European Council will wait for a report on this and the other aspects of the Energy Union by European institutions and Member States and will further comment on them in the meeting of the next December.

3 WTO framework applicable to EU trade in energy

The WTO legal framework in the field of energy is a disintegrated one. There are no specific rules on energy directly addressing its production, purchase and distribution, and even the word ‘energy’ is absent from the multitude of agreements composing the WTO system. The reason for this may be traced back to the historical roots of the organisation, with just a small number of producers of energy involved in the creation of the 1947 General Agreement on Tariffs and Trade (GATT) – the precursor of the WTO. Only more recently have major energy-producing States such as Russia and Saudi Arabia, together with some significant consumers like China or transit States like Ukraine, acceded to the WTO, amplifying a problem that is now strongly felt. This problem does not lie in the impossibility of applying WTO rules to energy-relating issues – this application is indeed absolutely possible – but in the fact that these rules were not tailored to energy, are incomplete and scattered throughout the WTO instruments. Incomplete because some topics are not covered (e.g., electricity as a non-storable, *sui generis* good has no status) or are covered in a general fashion, with no focus on energy problems (e.g., Art. V GATT on transit of goods is more basic than the relevant provision – Art. 7 – in the 1991 Energy Charter Treaty). Not-fully consistent because an activity like the transnational supply of energy is situated in the middle ground between the provision of a good (covered by the GATT) and of a service (covered by the General Agreements on Trade in Services; “GATS”), and ends up being subject to a dual regime⁴⁹.

This notwithstanding, there are many WTO rules that may find application in cases concerning energy resources. They range from the most-favoured-nation (Arts. I GATT, Art. II GATS) and the national-treatment principles (Art. III GATT, Art. XVII GATS)⁵⁰ to the prohibition of quantitative restrictions (Art. XI GATT), subsidies (Agreement on Subsidies and Countervailing Measures, hereinafter “ASCM”) and dumping (Anti-dumping Agreement; “ADA”). The reach from the rules on monopolies and State enterprises (Arts. II and XVII GATT, Art. VIII GATS) and technical obstacles to trade (Agreement on Technical Barriers to Trade) to those on the Agreement on Trade-related Investment Measures (“TRIMs”; e.g., local-content requirements) and the Agreement on Agriculture (biofuels). The functioning of many of these rules is well known in legal doctrine, so they will not be analysed in-depth here. Except for the Government Procurement Agreement – which is important since the greatest energy transactions are concluded through contracts between states and private companies – only a few elements will be discussed, as incidental to the main topics of this chapter, namely the fight against market distortions and the protection of the environment, two of the main political and legal challenges the EU is now facing.

3.1 The Revised Government Procurement Agreement

The 1994 GPA opens government-procurement among its parties by applying the non-discrimination principle (in both its most-favoured-nation and national-treatment aspects) to the goods and services provided to governments (Art. IV GPA). The agreement, being plurilateral, binds only the governments that have accepted it. All WTO members may accede to it. As of today, it covers 43 WTO members⁵¹ (counting the EU⁵² and its 28 member states). Another 28 WTO members and four international organisations participate in the GPA Committee as observers. At the moment, ten of them are negotiating accession, whereas five have undertaken commitments, in their WTO accession protocols, to

⁴⁹ Similarly, although in a different context, Panel Report, *China – Audiovisual* (WT/DS363/R).

⁵⁰ Both principles apply with reference to “like” products. It should be expected that different kinds of energy resources can be, at least to a little extent, deemed to be “like”, i.e. substitutable. The provision involved could also play a role: see AB Report, *Japan – Alcoholic Beverages* (WT/DS8/AB/R - WT/DS10/AB/R - WT/DS11/AB/R).

⁵¹ See www.wto.org/english/tratop_e/gproc_e/memobs_e.htm.

⁵² Council Decision 94/800/EC of 22 December 1994.

become parties. The negotiation of a Revised GPA was concluded in 2011 and the resulting text was formally adopted in 2012 and entered into force on 6 April 2014.

The GPA is composed mainly of two parts: the text of the Agreement and the parties' market access schedules of commitments. The principles and procedural requirements set out by the text of the Agreement do not automatically apply to all the procurement activities of each party. The GPA, in fact, does not apply to all the procurement activities of each party but only to those specified in the parties' coverage schedules⁵³. The GPA applies to contracts above certain thresholds, defined as special drawing rights. The agreement covers the procurement for governmental purposes of all goods and services procured by the entities listed in Annexes 1 through 3⁵⁴. With reference to the EU, Annex 1 contains the list of the 'central government entities' (both those of the EU and of the EU Member States) whose procurement is covered by the GPA, Annex 2 the list of the 'sub-central government entities'⁵⁵ and Annex 3 'all other entities'. In this last group fall all contracting entities whose procurement is covered by the EU Utilities Directive⁵⁶, which are contracting authorities (as in Annexes 1 and 2) or public undertakings⁵⁷. In particular, in the last category described in Annex 3 are included undertakings working in the field of 'the provision or operation of fixed networks intended to provide a service to the public in connection with the production, transport or distribution of electricity or the supply of electricity to such networks'⁵⁸. Moreover, in Annex 4 of the EU, included among the goods covered by the agreement are energy products such as: mineral fuels, mineral oils and products of their distillation, bituminous substances, mineral waxes, except special engine fuels (this denomination reflects the heading of Chapter 27 of the Harmonized System, which covers also electricity). There is no reference to energy services in Annex 5.

3.2 The EU, dual pricing and the fight against market distortions

3.2.1 The notion of dual pricing and the position of the EU

Dual pricing can be defined as the 'maintenance of prices for energy consumed domestically at a level below the global market price or the price at which the energy is sold for export'⁵⁹. No explicit prohibition of dual pricing exists in WTO law. This notwithstanding, since many are the commercial policies entailing dual pricing-like effects⁶⁰ it is possible to list a number of WTO provisions breached by this kind of practice: Art. III.9 GATT on internal maximum price control measures, Art. XI GATT on quantitative restrictions, Art. XVII GATT on state trading enterprises, as well as various provisions of the ASCM, the ADA

⁵³ A national security exception can be found in Art. III.1 GPA. In this respect the United States' schedule provides that the GPA does not cover: a) goods or services that support the safeguarding of nuclear materials or technology, if the procurement is conducted under the authority of the Atomic Energy Act; or b) any oil purchase related to the Strategic Petroleum Reserve.

⁵⁴ See www.wto.org/english/tratop_e/gproc_e/gp_app_agree_e.htm#revisedGPA for the schedules under the Revised GPA.

⁵⁵ See Regulation (EC) 1059/2003 of 26 May 2003 on the establishment of a common classification of territorial units for statistics, as last amended by Regulation (EC) 1137/2008, and the definitions of the Entities in Annex 2.

⁵⁶ Directive 2014/25/EU of 26 February 2014 on procurement in the water, energy, transport and postal services sectors.

⁵⁷ For a definition see Directive 2014/25/EU Art. 4(2).

⁵⁸ According to Annex 7 of the EU, "[p]rocurement by procuring entities covered under Annexes 1 and 2 in connection with activities in the fields of drinking water, energy, transport and the postal sector are not covered by this Agreement, unless covered under Annex 3".

⁵⁹ P. Milthorpe, D. Christy, *Energy Issues in Selected WTO Accessions*, in Y. Selivanova (ed.) *Regulation of Energy in International Trade Law. WTO, NAFTA and Energy Charter*, Kluwer, 2011, p. 271; one should note that some commodities, like oil, may be attributed a world market price, while others, like gas, may not.

⁶⁰ For example, export taxes (legal under Art. XI GATT), quantitative export restrictions (generally illegal under the same article), consumption subsidies (whose lawfulness depends on the conditions of their adoption) and, more specifically, the establishment by way of administrative decision of a maximum domestic price at a lower level than the export price (maybe a "pure" form of dual pricing).

and the TRIMs. In general, however, despite this abundance no unconditional support to the illegal nature of dual pricing can be found in the literature⁶¹.

In this context, the EU has tried to challenge the problem of dual pricing by following four different avenues. The first one is eliminating the ambiguity of existing WTO law, by providing answers to the problem of what is permissible within the WTO. For example, in 2006 the EU proposed to amend the rules on antidumping by recommending textual additions to Art. 3 ASCM⁶². This move must be framed in the broader picture of the Doha Round negotiations for a reshaping of the provisions of some WTO agreements⁶³. The current stalemate of the Round, however, makes this option hardly practicable.

Two more viable alternatives are those represented by the negotiation of ad hoc rules with the EU's trading partners, both inside and outside the WTO system. As far as bilateral accords are concerned, the best example is provided by the 2014 Association Agreement between the EU and Ukraine, whose Art. 270 – entitled 'Prohibition of dual pricing' – reads: 'neither Party or a regulatory authority thereof, shall adopt or maintain a measure resulting in a higher price for exports of energy goods to the other Party than the price charged for such goods when intended for domestic consumption'. An analogous solution is thought to be a possible outcome of the negotiations between the EU and the US on the Transatlantic Trade and Investment Partnership ('TTIP'), as the EU Commission is known to have circulated in 2013 to the US delegation a Position Paper suggesting the ban of dual-pricing policies. Indeed, the finding of an agreement with single states, both within and outside of the WTO, has been indicated as the main – and as of today, most practiced – solution to the dual pricing of raw materials⁶⁴.

As far as trade accords within the WTO are concerned, on the other hand, it must be noted that in recent years dual pricing has been addressed, more than once, in the accession agreement for new members of the WTO, thus giving rise to WTO+ obligations. For example, Saudi Arabia undertook certain commitments on the selling of NGLs⁶⁵, which are binding pursuant to Art. 2 of the 2005 Protocol of Accession⁶⁶. The same is valid for Russia, whose commitments relating to its gas market⁶⁷ are binding pursuant to Art. 2 of the 2012 Protocol of Accession⁶⁸. Thus, it would not be entirely correct to say that Russia managed to avoid undertaking WTO+ obligations on this regard⁶⁹. It is true, however, that the language of these commitments and the absence of an expressed deadline may raise doubts about the extent to which they are enforceable⁷⁰.

⁶¹ S. Ripinsky, *The System of Gas Dual Pricing in Russia: Compatibility with WTO Rules*, in *World Trade Review*, 2004; Y. Selivanova, *Energy Dual Pricing in the WTO: Analysis and prospects in the Context of Russia's Accession to the World Trade Organization*, Cameron May, 2008; V. Pogoretsky, *Energy Dual Pricing in International Trade: Subsidies and Anti-dumping Perspectives*, in Selivanova (ed.), *Regulation of Energy* cit.

⁶² Subsidies – Submission of the European Communities (TN/RL/GEN/135).

⁶³ See e.g., again on subsidies, the New Draft Consolidated Chair Texts of the AD and SCM Agreements of December 2008 (TN/RL/W/236), especially Arts. 2.1 and 14 of the Draft ASCM.

⁶⁴ Opinion of the EU Economic and Social Committee on 'Securing essential imports for the EU through current EU trade and related policies' (OJ C 067, 06.03.2014); Reply of Mr De Gucht to a question of Mr Caspary, in OJ CE 219, 31.07.2013.

⁶⁵ Para. 33 of the Report of the Working Party on Accession (WT/ACC/SAU/61).

⁶⁶ Protocol of Accession of Saudi Arabia (WT/L/627): "This Protocol, which shall include the commitments [taken by Saudi Arabia], shall be an integral part of the WTO Agreement". This notwithstanding, still in 2012 the matter was subject of debate at the WTO, with Saudi Arabia rejecting the idea of it being practicing dual pricing (WT/TPR/M/256/Add.1).

⁶⁷ Report of the Working Party on Accession (WT/ACC/RUS/70 - WT/MIN(11)/2), paras. 132 and 133.

⁶⁸ Protocol of Accession of the Russian Federation (WT/MIN(11)/24 - WT/L/839).

⁶⁹ Pogoretsky (Energy Dual Pricing cit.) informs that 'Russia has contested any commitments in relation to domestic energy policy during its WTO accession negotiations' (p. 184), and that its plan to converge export and domestic gas prices is mainly due to financial concerns rather than legal obligations (p. 189). According to G. Horlick, the outcomes of the negotiations of Russia's and Saudi Arabia's WTO accessions are 'somewhat uncertain' (in J. Pauwelyn (ed.), *Global Challenges at the Intersection of Trade, Energy and the Environment*, Centre for Trade and Economic Integration, 2010, p. 202).

⁷⁰ For the notion of WTO+ obligations see *infra*, footnote 96 at the beginning of the next chapter.

The fourth avenue available to the EU is the exploitation of the existing WTO legal framework and, despite its deficiencies, the recourse to antidumping measures. The Union has taken this path with conviction. According to the latest Annual Report of the European Commission on the EU's Anti-Dumping Activities, of 31 December 2013 there were several definitive anti-dumping measures in force, some of them regarding energy-intensive products profiting from dual-pricing national policies⁷¹. The EU has made clear its intention not to underestimate the risks these practices pose to its economy, and its willingness not to apply the so-called lesser duty rule⁷² according to which '[t]he amount of the [...] anti-dumping duty [...] should be less than the margin [of dumping] if such lesser duty would be adequate to remove the injury'⁷³. However, questions concerning the consistency of these measures with WTO law have been raised by many.

3.2.2 Anti-dumping rules: an effective strategy against dual pricing policies?

In order to challenge these measures, Russia sought consultations in 2014 with the EU on 'cost adjustment methodologies and certain anti-dumping measures on imports from Russia', and filed a request for the establishment of a panel⁷⁴. In July 2014, the Dispute Settlement Body (DSB) established the panel. As the title of the claim suggests, the focus is on how the magnitude of the dumping by Russian energy-intensive goods sold in the territory of the EU is calculated by European authorities. On the one hand Regulation No. 1225/2009 adds some text to the provisions of the ADA (the consistency of the former with the latter being debatable), while on the other hand, the ADA itself is not without opacity as to its requirements.

The ADA deems a product as being dumped if the 'price of the [exported product] is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country' (Art. 2(1)). Under certain factual circumstances, though, different methods of calculation may be used, i.e. 'because of the particular market situation'⁷⁵. In these cases, the margin of dumping shall be determined by comparison with the 'price of the like product when exported to an appropriate third country [or] the cost of production in the country of origin plus a reasonable amount for administrative, selling and general costs and for profits'⁷⁶. These costs 'shall normally be calculated on the basis of records kept by the exporter [...], provided that such records [...] reasonably reflect the costs associated with the production and sale of the product'⁷⁷.

Two problems arise here. One is related to the notion of 'reasonable reflection of the costs', which is not further explained in the ADA. The EU believes that a reasonable reflection should incorporate in the costs of the end-product also the non-dumped costs of input-products, i.e. the instrumental goods necessary for the production (input dumping). Since energy is an important input for energy-intensive products, the purchase of energy at dumped or below-cost prices is deemed by the EU not to adequately reflect the costs associated with production. However, the WTO law does not take any stance on calculating the margins of dumping taking into account input dumping. In 1984, a WTO committee tried to address the

⁷¹ 32nd Annual Report from the Commission to the Council and the European Parliament on the EU's Anti-Dumping, Anti-Subsidy and Safeguard Activities (SWD(2015) 10 final). At the end of 2013, 86 anti-dumping measures and 12 countervailing measures were in force. Many of them concerned energy-intensive products (basic chemicals, iron and steel goods, ceramic, glass, paper, etc.), i.e. those which would benefit most from a dual pricing policy.

⁷² Art. 7(2) of EU Council Regulation No. 1225/2009, the legal text that incorporates the ADA in the European system.

⁷³ This position was expressed at the end of 2013 during the EU trade-policy review (WT/TPR/M/284/Add.1/Rev.1).

⁷⁴ Request for the Establishment of a Panel, *European Union – Certain Adjustment Methodologies* (WT/DS474/4). Many States, including some practicing or having practiced dual pricing or policies with a similar effect, reserved their third-party rights.

⁷⁵ Art. 2(2) ADA, which does not clarify the expression 'particular market situation'. The EU Regulation No. 1225/2009 specifies: 'when prices are artificially low' (Art. 2(3)). On the notion of market situation, see also below.

⁷⁶ Art. 2(2) ADA.

⁷⁷ Art. 2(2)(1)(1) ADA.

issue – contrary to what has been argued⁷⁸, its recommendations can hardly be seen as impeding a calculation on an input-dumping basis under particular circumstances⁷⁹ – but the document it produced is likely to be of little value. As a consequence, basing the calculation of the margin of an industry's undue economic advantage on the 'theory' of input dumping certainly entails a risk for this practice to be challenged under WTO law.

The other problem regards the consequences of a declaration of 'unreasonable reflection of costs'. Again, WTO law is silent. Art. 2(5) of the Regulation No. 1225/2009 fills this gap in the ADA by allowing unreasonable costs to be adjusted 'on the basis of [...] information from other representative markets'. The EU has often chosen this option, which, however, apparently runs counter to Arts. 2(2) and 2(2b) ADA, in so far as both articles prescribe the use of a country-of-origin benchmark. This point, too, is object of firm contestation on the part of Russia.

As we have briefly seen above, the conditions of the market in which companies accused of dumping practices operate may affect the way the margin of dumping is calculated. The concepts of 'ordinary course of trade' and 'particular market situation' – similarly to that of 'commercial considerations' in Art. XVII GATT – assume market-oriented actors to be the ordinary players of Member States' economies. Whenever this is not the case, consequences follow. Art. 2(7) ADA affirms that the provision in which it is contained is without prejudice to Article VI in Annex I to GATT 1994 on non-market economies, and allows for deviation from a strict comparison with domestic prices when calculating the dumping margin. The definition of non-market economy, however, is stringent ('a country [...] where all domestic prices are fixed by the State'), and nowadays very few states fit this description. Moreover, in 2002 Russia was granted market-economy status by the EU, although it should be noted that this graduation does not compel WTO judicial bodies.

In principle the possibility exists for a particular interpretation of Article VI of Annex I, so that the price control may only occur in a specific sector, e.g. the gas market (which, in the anti-dumping cases against Russia, is the market of a relevant input-product). This solution has been envisaged, although apparently in relation only to the end-product, by the 2001 Protocol of Accession of China⁸⁰, which permits the use of a third-country benchmark 'if the producers under investigation cannot clearly show that market economy conditions prevail in the industry' of the like product. Attention must be paid, however, to the imminent cessation of this legal regime, as the Protocol defines it as only fifteen-years long, although it is not clear what is going to happen when, at the end of 2016, this period will expire. Opinions are polarised between those believing that China will automatically acquire a market status and those convinced that the EU will still be entitled to consider, on a case-by-case basis, the author of an alleged dumping as acting in a non-market environment⁸¹. Commissioner Malmström affirmed in December 2014 that China cannot expect to automatically receive market economy status, as this can only be attained by complying with the requirements set out in Art. 2(7) of Regulation No. 1225/2009. China filed an application under Art. 2(7) in 2004, but EU authorities report that as of 31 December 2013 the last report shared with the Chinese authorities is dated 2008.

⁷⁸ Pogoretsky, *Energy Dual Pricing* cit., p. 219.

⁷⁹ Draft Recommendation Concerning Treatment of the Practice Known as Input Dumping (ADP/W/83/Rev.2), para. 6.

⁸⁰ Protocol of Accession of the People's Republic of China (WT/L/432), para. 15(ii).

⁸¹ See, on this topic, the debate hosted by the *Global Trade and Customs Journal*, 2014 (Issue 4).

3.3 The EU, trade in energy and the environment

3.3.1 Subsidies as ‘friends’ and ‘enemies’ of the environment

The WTO regime for subsidies is spread throughout the WTO treaties. Art. 16 GATT and Art. 15 GATS provide the general framework for goods and services, but what they prescribe does not go beyond mere duties of notification or negotiation. More articulated rules may be found in the Agreement on Agriculture and, of course, the ASCM. The former identifies three types of subsidies, of which none is strictly prohibited: consequences range from the duty to minimize subsidies to the possibility to their unlimited use. To this last category belong those subsidies that, lacking a distorting effect on trade, also set in motion policies deemed worthy of being promoted: according to Art. 2(a) of Annex 2, ‘research in connection with environmental programmes’ is one of them, and there is perhaps reason to think that subsidised cultivation of biofuels could be possible.

As to the ASCM, it bans subsidies that are declared ‘prohibited’ (Art. 3 ASCM): that is, that are contingent upon an export performance or the use of domestic over imported goods. This latter condition is quite common in the case of subsidies granted to renewable energy sources – apparently, much more common than in the case of subsidies to fossil fuels, so that the former more than the latter run the risk of being challenged for breaching Art. 3 ASCM⁸². In 2012, for example, the EU was brought before a WTO panel by China on the basis of similar allegations⁸³. The overall result is that subsidies often practically end up favouring the use of polluting resources.

If a subsidy cannot be classified as prohibited, and in the case it is ‘specific’, it only entitles injured states to take countervailing measures. It will often prove difficult to successfully challenge a subsidy under the WTO law. Moreover, although the agreement is a very detailed one, it leaves the door open to the enactment of policies which are not subsidies under the ASCM but have similar effects. For instance, import tariffs (which are legitimate in the WTO) may result in the domestic producers raising their prices and gaining more at the expense of their foreign competitors: a gain that can be seen as a sort of ‘legitimate’ subsidy⁸⁴.

3.3.2 The forthcoming Environmental Goods Agreement

Also of relevance is the Environmental Goods Agreement, now discussed as part of the Doha Round of negotiations (on which agreement is supposed to be reached by July 2015). The Agreement aims at identifying a list of products serving environmental purposes – e.g., wind turbines and solar panels – and reducing their custom duties to zero. The tariff reductions flowing from this plurilateral agreement would be made on a most-favoured-nation basis, thus benefitting all WTO Members. It has been noted however that, even if there were a long list of products covered the economic impact would be relatively small⁸⁵. Moreover, a number of issues are not going to be resolved, such as non-tariff barriers, environmental services (originally envisioned in the Doha mandate) and dual-use goods (i.e., goods that have both environmental and non-environmental purposes, like pipes).

3.3.3 Protection(ism) of natural resources and its effects

Protectionism is the sworn enemy of the WTO, and protection of legitimate interests (such as environmental ones) may be easily confused with that of illegitimate interests. Exceptions to the full

⁸² T. Meyer, *Energy Subsidies and the World Trade Organization*, ASIL Insights, 2013.

⁸³ *EU and Certain Member States – Renewable Energy* (WT/DS452/1 - G/L/1008 - G/SCM/D95/1 - G/TRIMS/D/34).

⁸⁴ R. Steenblick, *Subsidies in the Traditional Energy Sector*, in Pauwelyn (ed.), *Global Challenges* cit., pp. 184-185.

⁸⁵ J. de Melo, M. Vijil, *The Critical Mass Approach to Achieve a Deal on Green Goods and Services: What is on the Table? How Much to Expect?*, Ferdi Working Paper 107, 2014.

liberalization of trade exist and have been invoked in WTO case-law quite often. However, they are somewhat strictly applied. As far as trade in natural resources is concerned, only a couple of exceptions explicitly refer to the environment: Arts. XX(b) GATT (measures 'necessary to protect human, animal or plant life or health') and XX(g) GATT (measures 'relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption')⁸⁶. Whether this is bad for the environment depends on the circumstances of a case. In fact, three possible situations can be envisaged. First, the object of protection through the resort to a WTO exception could be a comparatively high-polluting resource, like oil⁸⁷. Second, a state could be willing to protect a comparatively low-polluting resource, like methane. Third, the exception could be used to safeguard non-energy resources that are instrumental to the production of low-polluting or renewable energies, as is the case for some raw materials⁸⁸. Of course, in the last two cases the successful invocation of exceptions to export-relating obligations might have detrimental effects on the environment. This could bring to a clash of conflicting – and both legitimate – environmental interests: those of the state invoking the exception and those of the state which considers it as an undue obstacle to the promotion of green energies.

The third example resembles what happened in a pair of recent cases – very similar in the judicial conclusions expressed by WTO organs – brought by the EU to the DSB⁸⁹. In both cases the respondent was China, which was found to be responsible of a breach of its obligations by granting its domestic industries preferential access to some resources by means of export duties (generally acceptable under the WTO law but specifically excluded by the Protocol of Accession of China), export quotas and other non-tariff barriers. The reasons for this decision were multiple. In the first place, Arts. XX(b) and XX(g) were deemed to be inapplicable to WTO+ obligations like those consisting of the prohibition of export duties, since the scope of the exceptions does not reach obligations contained in single instruments of accession⁹⁰. In the second place, it has to be noted that, despite an apparently plain text, exceptions provided for in GATT are not easily interpreted: for example, the meanings of 'disguised restriction on international trade' ('Chapeau' of Art. XX GATT); 'necessary' (Art. XX(b) GATT) 'relating to' and 'made effective in conjunction with' (Art. XX(g) GATT). As a consequence, it can prove quite hard to foresee how far a WTO member can go in protecting its own resources.

This protection can be afforded not only, as above, by means of restricting exports, but also by setting a series of requirements a foreign state must comply with in order to be able to trade in energy resources⁹¹. This issue is generally addressed by the Agreement on Technical Barriers to Trade, which tries to minimise the impact of such regulations. Sometimes the distinction between regulations and straightforward prohibitions is a fine line. For example, in the case of the 1938 US Natural Gas Act, Art. 3 makes the exportation of gas dependent on a decision of US authorities regarding its consistency with the US public interest – a consistency which is taken for granted if the counterpart is party to a free trade agreement

⁸⁶ An identically-phrased provision with respect to Art. XX(b) GATT exists in GATS (Art. XIV(b)). No provision on the preservation of natural resources is present; however, Art. XIV(c)(3) generally speaks of measures relating to 'safety'.

⁸⁷ Export restrictions have been routinely applied by the OPEC countries – and they have never been challenged. There are authors who believe that there is ground for such a challenge: P.D. Farah, E. Cima, *Energy Trade and the WTO: Implications for Renewable Energy and the OPEC Cartel*, in *Journal of International Economic Law*, 2013.

⁸⁸ One could think also to biofuels, which, being produced from food, are probably better covered by Art. XI(2)(a) GATT.

⁸⁹ AB Report, *China – Raw Materials* (WT/DS395/AB/R) and AB Report, *China – Rare Earths* (WT/DS432/AB).

⁹⁰ This is the argument that attracted most criticism: see, *inter alia*, J.Y. Qin, *Judicial Authority in WTO Law: A Commentary on the Appellate Body's Decision in China-Rare Earths*, in *Chinese Journal of International Law*, 2014. See also, in general terms, in L. Ehring, G.F. Chianale, *Export Restrictions in the Field of Energy*, in Selivanova (ed.), *Regulation of Energy* cit., pp. 120-125.

⁹¹ Incidentally, it may be noted that the European Union itself adopts policies allegedly discriminating between EU and non-EU energy providers, thus possibly protecting its market from foreign competition. The EU Third Energy Package has been challenged by Russia within the WTO on the basis of similar allegations: *EU and its Member States – Certain Measures Relating to the Energy Sector* (WT/DS476/1 - S/L/409 - G/L/1067 - G/SCM/D102/1 - G/TRIMS/D/40).

with the US. Two issues arise here.. One relates to the principle of non-discrimination, which may be incompatible with the preferential treatment granted to parties PTAs. This objection may perhaps be countered on the basis of the Art. XXIV GATT exception to MFN, which is not closely defined. The other relates to the nature of Art. 3, which might be seen as imposing a de facto, if not de jure, obstacle to trade that is difficult to justify on the basis of Art. XX GATT or even Art. XXI GATT (security exceptions).

As stated above, protectionism might be used to pursue environmental objectives, if aimed at preventing the depletion of natural resources. Moreover, a state might decide to protect resources relating to the production of renewable energy by prohibiting or discouraging their exports. This has the effect of isolating them from external demand, reducing their prices and, as a possible consequence, promoting their usage for domestic production of green energy. Of course, in practice the contrary is also often true. Trade in resources that are instrumental to the production of renewable energy may have an effect similar to the liberalization of trade in polluting resources, i.e. making the production of green energy comparatively more costly. This is so because the supply of resources necessary to produce green energy decreases, whereas the demand does not. Moreover, this effect is amplified by the fact that very often renewable energy production is, from the start, not economically profitable and needs to be sustained by state policies. This is, per se, a problem, since not every kind of support is legal under international trade law⁹², and granting subsidies⁹³ as well as rolling them back⁹⁴ may entail a breach of current regulation.

4 EU commercial policy and WTO+ rules

The adoption of the Treaty of Lisbon represented a fundamental change to EU commercial policy both on substantive and procedural grounds. In terms of substance EU commercial policy is not merely aimed at liberalising trade (Art. 206 TFEU), but is subordinated to the general values, interests and foreign policy objectives of the Union (Arts. 206, 207 TFEU). On procedure, the EU Parliament has become a 'veto player' in the adoption of the relevant legislation. The Treaty also attributed a new competence to the EU in the area of investment (Art. 207(1) TFEU). As noted above the Treaty is equally significant for the development of an EU energy policy. For the first time, Members States decided to include a specific provision defining a common policy in the field of energy⁹⁵.

Against this background, the aim of this chapter is to describe and assess the main tenets of EU commercial policy in the energy sector. Our analysis will focus on the most important development in this field, that is, the conclusion of a network of new generation Free Trade Agreements (FTAs). Such legal instruments are mainly aimed at complementing the WTO regulation with, *inter alia*, rules on the protection of investments. In light of their function and nature, they are generally dubbed 'WTO+' rules⁹⁶.

4.1 New generation FTAs: An overview

With the beginning of the new millennium, as the prospects for the success of an ambitious multilateral WTO Round diminished, the trade policy of the EU gradually shifted towards a wider use of bilateral or

⁹² For a review of lawful, unlawful and dubious measures see S. Charnowitz, *Green Subsidies and the WTO*, World Bank Policy Research Working Paper 7060, 2014, pp. 39 ff.

⁹³ See above, footnote 83.

⁹⁴ For example, Spain, Italy and the Czech Republic have faced or are now facing investors' claims in many fora: R.W. Thorn, *Renewable Energy Policy Changes Lead to Damages Claims – Investment Treaties, European Feed-In Tariffs, Arbitration, Political Risk, Expropriation*, available at www.chadbourn.com/renewable_energy_policy_changes_june2014_projectfinance/.

⁹⁵ See Chapter 2.

⁹⁶ In this chapter, with the phrase WTO+ rules we do not refer to the additional commitments that some LDC countries had to accept at the moment of accession to the WTO. We use the phrase in a more colloquial form, with reference to agreements stipulated outside the WTO system that foster the attainment of the trade objectives of the parties. As it has been noted: 'The term can be used with reference both to trade-related issues that are outside the scope of the WTO negotiations (e.g., foreign direct investment, labour mobility, environmental issues and regulatory harmonisation) and questions within the scope of the WTO (e.g. ,trade in services) but where trade agreements outside of the WTO have adopted an approach superior to that used in the WTO': S. Gstohl, D. Hanf, *The EU's Post-Lisbon Free Trade Agreements*, *European Law Journal*, 2014, pp. 744-745.

regional FTAs⁹⁷. The situation evolved up to the point that ‘there are currently merely eight members of the WTO that trade with the EU on the basis of most-favoured nation treatment’⁹⁸. As a result, the EU has today 50 preferential agreements in place and is negotiating with about 12 other countries⁹⁹. Obviously, these instruments are very diversified: some of them are defined as Economic Partnership Agreements, some others as Association Agreements, still some others are merely referred to as Free Trade Agreements¹⁰⁰. In this context, the EU post-Lisbon commercial policy is characterised by the emergence of the so-called ‘new generation’ FTAs. Such instruments target not only tariff barriers to trade in goods, but also a wider array of sectors such as non-tariff barriers, services, investment, public procurement, and intellectual property rights. Some of them also establish an investor-state dispute settlement (ISDS) mechanism, which grants the investor the right to claim compensation through the establishment of an arbitration panel¹⁰¹.

Among the FTAs currently in the process of being negotiated or recently adopted, the EU-Canada Comprehensive Economic and Trade Agreement (CETA) and the EU-United States Transatlantic Trade and Investment Partnership (TTIP) stand out for their potential relevance to the energy sector. The endowment in natural resources of the interested countries coupled with the importance of the economic interchange between those countries and the EU speak for themselves. As will be seen, however, other FTAs can also have an impact on the energy sector¹⁰².

Before addressing the relevance for energy of the new generation FTAs it is worth noting, however, that the EU and its member states are also parties to a multilateral agreement that, while being extraneous to the WTO system, is fairly relevant to the energy sector: the Energy Charter Treaty (ECT). This treaty, which entered into force in 1998, covers a number of provisions: it protects and promotes foreign investments in the field of energy based on the extension of national treatment or on the most-favoured-nation treatment; it promotes a predictable framework for trade in energy products and energy-related equipment; it also promotes freedom of energy transit through pipelines and grids. In sum, with relation to trade in energy goods, the ECT mirrors the WTO core principles and complements them with the protection of investments in energy and the presence of the ISDS system.

4.1.1 On the territorial extension of the FTAs: Do they cover the exclusive economic zone and the continental shelf?

An issue worth being explored is the geographical scope of application of the FTAs. The text of the chapter on investment of CETA clarifies that its geographical scope covers the *exclusive economic zone* (EEZ) and the *continental shelf* of the parties to the exclusion of overseas countries and territories¹⁰³. This is a significant statement, especially with regards to the protection of foreign investment. There is no doubt that activities such as the drilling of the subsoil in the EEZ and/or the continental shelf will be covered by the agreement¹⁰⁴. However, there are details that require some clarification. Firstly, it should be stressed that the EU, as an international organization, does not have an EEZ or a continental shelf. For

⁹⁷ S. Woolcock, *European Union Policy Towards Free Trade Agreements*, ECRE Working Paper, No. 3/2007.

⁹⁸ S. Gstohl, D. Hanf, *The EU's Post-Lisbon*, cit., p. 733.

⁹⁹ *Ibidem*.

¹⁰⁰ The concept of Deep and Comprehensive Free Trade Agreements (DCFTAs) will be addressed in the ensuing chapter.

¹⁰¹ See below, Section 4.2.1.

¹⁰² See, for instance, the agreement with Singapore and the agreement with Korea referred to in Section 4.2 below.

¹⁰³ CETA, Investment, Art. X.1.

¹⁰⁴ Even in the absence of such specification, the same conclusion could perhaps be reached on the basis of an argument of functional analogy. Since States exercise in those maritime zones sovereign powers over natural resources that – at least in some respects – can be equated to sovereignty, EU law applies in those areas within the limits of the allocation of competences between member States and the Union itself. See Court of Justice of the European Union, 17 January 2012, *Salemink*, C-347/10, EU:C:2012:17, para. 35.

the purposes of the FTAs, the EEZ and the continental shelf 'of the EU' is indeed the EEZ and the continental shelf of its member states. In this respect, whereas the continental shelf is a geological concept that automatically pertains to each coastal state, the EEZ is a legal concept and requires its establishment through an official act of the concerned state. Not all of the member states of the EU, and this is particularly true for the Mediterranean states, have established an EEZ. Secondly, it is important to note that neither the EU treaties, nor the FTAs, may have an impact on the decision of the coastal states on whether the hydrocarbon resources located offshore shall be explored or exploited. In this respect, Art. 194(2) TFEU introduces a clear *caveat* with reference to the energy policy of the EU: 'Such measures shall not affect a Member State's right to determine the conditions for exploiting its energy resources, its choice between different energy sources and the general structure of its energy supply'. In conclusion, it can be said that the decision as to whether the resources shall be exploited pertains to the sovereign rights of the member states of the EU. However, once an authorization to operate in the EEZ is granted, economic activities carried out thereafter will be fully protected by the agreement.

4.2 New generation FTAs and their impacts on the energy sector

The relevance of the new generation FTAs to the energy sector must be addressed on different levels. As concerns their trade dimension, the significance of the FTAs to the energy sector is not really related to the elimination of import duties that are often negligible. Their relevance is rather connected to: (a) the reduction of technical barriers to trade in energy materials, (b) the elimination of export duties on energy resources and (c) the opening of new business opportunities in the provision of services or in government procurement.

One of the most relevant examples of option (a) regards the elimination of technical barriers to trade and investment in equipment aimed at generating renewable energy. With relation to such equipment, in the EU Singapore FTA (EUSFTA) it is stated that, on the one hand, 'the Union will accept declarations of conformity from Singapore suppliers under the same terms as from Union suppliers for the purpose of placing such products on the market'¹⁰⁵, and that, on the other hand, 'Singapore will accept EU declarations of conformity or test reports, for the purpose of placing such products on the market without any further requirements'¹⁰⁶. Pursuing the same *rationale* of opening up local markets, one might also quote the prohibition of adopting measures on local content requirements in goods, services and investments¹⁰⁷.

Although the draft of the TTIP treaty is not officially available to the public, the position of the EU is that the final text should contain similar provisions with respect to energy efficiency and the promotion of renewable energies. According to the Commission '[t]he TTIP should promote the objective of renewable energy and energy efficiency and should guarantee the right for each party to maintain or establish standards and regulation [...], while working, as far as possible, towards a convergence of domestic EU and US standards or the use of international standards where these exist'¹⁰⁸.

On the abolition of export duties and quotas on energy resources, it goes without saying that this represents a strategic objective for an actor concerned with energy security such as the EU. Indeed, the lifting of national restrictions to the export of US oil and liquefied natural gas (LNG) to the EU seems to be one of the most important objectives in the EU's negotiating position on TTIP¹⁰⁹. There is no doubt that

¹⁰⁵ EUSFTA, Chapter VII, Art. 7.5(3)(a).

¹⁰⁶ EUSFTA, Chapter VII, Art. 7.5(3)(b).

¹⁰⁷ EUSFTA, Chapter VII, Art. 7.4(a).

¹⁰⁸ EU-US TTIP, Raw Materials and Energy – Initial EU Position Paper, at: http://trade.ec.europa.eu/doclib/docs/2013/july/tradoc_151624.pdf.

¹⁰⁹ S. McKeagney, Proposal reveals EU pressure on US to lift ban on crude oil exports, in *The Washington Post*, 9 July 2014.

this position appears to contribute to one of the objectives of the energy policy mentioned above, namely to 'ensure the security of supply in the Union' *inter alia* through a diversification of energy sources and their origin. The other side of the coin, however, is that a policy aimed at favouring the import of resources with a high carbon footprint – such as for instance LNG obtained from fracking – might be incompatible with the principles set by the general provisions on the Union's external action with regards to the protection of the environment¹¹⁰. The whole issue, however, could turn out to be largely theoretical as there are doubts that the import of US oil and LNG would significantly alter Europe's energy balance¹¹¹.

Finally, two other areas of the FTAs intersecting energy concern the provisions on government procurement and services. As discussed in the previous chapter, the essence of the provisions liberalising government procurement is non-discrimination, in the sense that public entities shall not treat foreign tenders less favourably than local ones. It is quite clear that this principle is of immediate relevance to corporations operating in the energy sector. Indeed, the CETA brings about important novelties in this field. In contrast to the WTO GPA Agreement¹¹², the Canadian sub-federal levels and public utilities such as Ontario Power Generation, Labrador Hydro, and others will have their contracts awards and procurement procedures scrutinised under the agreement¹¹³.

In an issue that has been generally overlooked is the provision on labour mobility that facilitates the right to enter and work temporarily for skilled professionals. In the case of CETA these provisions can be directly relevant to the extractive sector considering that: a) there are European corporations operating in the extractive industry in Canada (and vice versa)¹¹⁴ and b) the mining industry always requires high skilled professionals.

4.2.1 Protection of investments in post-Lisbon FTAs

In addition to the regulation of trade in energy related products and services, the most significant feature of (some of) the post-Lisbon FTAs is foreign investment protection. This aspect can be crucial in the energy sector, where investment is normally very large and investors often risk being trapped as a result of high sunk costs¹¹⁵. The approach taken by the EU in this respect is not always uniform, but it is somewhat innovative: the main principles of international investment protection that are usually found in most Bilateral Investment Treaties (BITs) are mirrored in the text of the EU agreements, but their content is clarified in an effort to increase predictability and legal certainty. For instance, the EU-Korea FTA makes reference to the MFN clause and to national treatment¹¹⁶, but does not mention protection from expropriation and the fair and equitable treatment standard (FET)¹¹⁷. The definition of the MFN, moreover, is conditioned upon a number of additional requirements and exemptions. In substantive terms, EUSFTA and CETA provide significantly wider protection to foreign investors, making reference not only to the MFN clause, but also to FET, expropriation and national treatment. Also in these two treaties, one might note that the drafters did put significant effort in narrowing down the otherwise vague fundamental concepts of international investment law.

¹¹⁰ Art. 21(2)f TEU reads: 'help develop international measures to preserve and improve the quality of the environment and the sustainable management of global natural resources, in order to ensure sustainable development'.

¹¹¹ I. Dreyer, *TTIP and Europe's energy question*, 4 June 2014 (www.borderlex.eu/comment-ttip-europes-energy-question).

¹¹² Coverage Schedules under the Revised GPA, Annex 5, at: www.wto.org/english/tratop_e/gproc_e/gp_app_agree_e.htm.

¹¹³ Consolidated CETA Text, Canadian Government Procurement Market Access Offer, at: www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/ceta-aecg/text-texte/21_01.aspx?lang=eng.

¹¹⁴ US-EIA, Canada Report (2014), at: www.eia.gov/countries/analysisbriefs/Canada/canada.pdf.

¹¹⁵ See the WTO Report on Trade in Natural Resources (2010), p. 183.

¹¹⁶ EU-Korea FTA, Arts. 7-6, 7.13.

¹¹⁷ J. Harrison, *The Legal Framework for Investment Protection between the European Union and Korea: Towards a Level Playing Field for Investors*, in J. Harrison (ed.), *The European Union and South Korea*, EUP, 2013, pp. 102-123.

Under both a political and a legal perspective, however, the most important (and hotly debated) aspect of investments under the FTAs regards the possible inclusion in the treaties of an ISDS system for the settlement of disputes. In recent agreements and negotiations the EU has clearly supported the adoption of the investor-state system for the settlement of disputes. An ISDS clause has been inserted in the text of EUFSA, CETA, and is currently being discussed in the negotiations of TTIP.

As shown by recent practice concerning other investment treaties, investor-state arbitration has been widely used in the energy sector. In one of the most debated cases, the ISDS clause in the ECT has allowed Vattenfall, a firm operating in the field of nuclear energy, to sue the German government for its decision to shut down two of the oldest reactors after the events in Fukushima¹¹⁸. In another emblematic case, Lone Pine Resources challenged under the NAFTA the moratorium on fracking adopted by Quebec and the subsequent revocation of its gas and oil exploration permits¹¹⁹.

Theoretically, the rationale of the ISDS system lies in the need to provide stability to foreign investors by shielding them from the abusive behaviour of the host state. By reducing the political risk of the investment, the ISDS clause enhances its efficiency benefiting both the investor and the host State. When compared for instance with the WTO dispute settlement system, the ISDS clause reveals several peculiarities: the settlement takes place at the investor-state level and not at the inter-state one; arbitrators are selected by the parties on a case by case basis; transparency of the proceedings is not necessarily the rule, but depends on the will of the parties; there is no 'judgment' of appeal; the proceedings do not merely aim at bringing the unlawful conduct to an end but also provide for compensation for the damage allegedly suffered by the investor. Moreover, when compared with judicial proceedings taking place in developed, rule of law legal systems, the ISDS system shows important deficiencies such as the absence of a set of enforceable rules on the impartiality of arbitrators; problems of consistency and erroneous decisions; absence of transparency and legitimacy. In sum, the question can be asked whether 'three individuals, appointed on an ad hoc basis, can be seen by the public at large as having sufficient legitimacy to assess the validity of States' acts, particularly if the dispute involves sensitive political issues'¹²⁰.

Faced with strong criticism from both civil society and academic circles, the EU has chosen to act in two separate but related directions. On the one hand, as mentioned above, the substantive rules of international investment law inserted in the most recent FTAs have been clarified to reduce interpretive discretion. On the other, provisions aimed at improving the functioning of the ISDS system have been drafted. They aim *inter alia* at discouraging tactical claims by making the loser pay all of the costs; increasing transparency by publishing the documents for the case; granting access to hearings to interested parties like NGOs; reducing conflicts of interest among arbitrators by adopting a code of conduct; setting up an appeals system to increase consistency in the results¹²¹. It remains to be seen whether these improvements will be effective in tackling the deficiencies of the ISDS system. A recent public consultation launched by the

¹¹⁸ N. Bernasconi-Osterwalder M.D. Brauch, *The State of Play in Vattenfall v. Germany II*, IISD Briefing Note, December 2014, at: www.iisd.org/sites/default/files/publications/state-of-play-vattenfall-vs-germany-ii-leaving-german-public-dark-en.pdf.

¹¹⁹ Another case concerns the moratorium on off-shore wind farms adopted by the Ontario Power Authority. Pending research on their health effects, it has been challenged on the grounds that it would have been in conflict with NAFTA's provisions on expropriation and fair and equitable treatment. Moreover, in 2013, some thirteen new cases were brought against the Czech Republic and Spain for issues related to the withdrawal of their programmes for subsidies to renewable energy under the applicable bilateral investment treaties. See: UNCTAD, IIA Issues Note, Recent Development in Investor-State Dispute Settlement, No. 1 April 2014, at: http://unctad.org/en/publicationslibrary/webdiaepcb2014d3_en.pdf.

¹²⁰ UNCTAD, UNCTAD Series on Issues in International Investment Agreements, New York and Geneva, 2014, 25, at: http://unctad.org/en/PublicationsLibrary/diaeia2013d2_en.pdf.

¹²¹ Investment Protection and Investor-to-State Dispute Settlement (ISDS) in EU Agreements, EU Commission Fact Sheet, March 2014, at: http://trade.ec.europa.eu/doclib/docs/2014/march/tradoc_152273.pdf. See also: CETA, Rules of Procedure and Code of Conduct, Annex I.

EU Commission has shown that European public opinion is clearly opposed to the ISDS clause and Commissioner Malmström expressed her readiness to take these concerns into account¹²².

4.3 Protection of investments in highly corrupted states

A substantial amount of the production of oil and gas originates from developing countries¹²³. These generally have weaker institutions and instruments to combat corruption than many industrialised countries. The problem is amplified by the fact that the energy sector attracts huge amount of investment and thus makes bribery even more likely. However, in the last twenty years there has been a multiplication of regional and global efforts to fight the phenomenon of corruption through treaties and other measures¹²⁴. Although similar, these acts vary considerably and provide for different types of obligations. In particular, the United Nations Convention against corruption¹²⁵ is aimed at the prevention of the phenomenon, its criminalization at the national level, the improvement of international cooperation and, last but not least, asset recovery. Investors in the energy sector are at the same time victims and culprits of this phenomenon, but this dual role is generally not recognised by the investment protection regime, which tends to charge more the author of a corruptive act than the authority that may have solicited it. This is the jurisprudential trend that, in the paucity of references to corruption in the BITs¹²⁶, has utilised rules not related to corruption in order to sanction the illicit behaviour of the corruptor. As many bilateral investment treaties include clauses that make the protection of economic activity dependent upon compliance with the laws of the host country¹²⁷, the argument has been made that an investment tainted by bribery cannot have been made 'in accordance with the law'. In this case, the consequence is the voidability of the contract or at least the impossibility to invoke protection under the investment treaty (be it on the ground of inadmissibility or lack of jurisdiction)¹²⁸. An innovative method of tackling the problem of corruption might be found in initiatives aimed at promoting revenue transparency and the disclosure of payments to governmental authorities either at the level of the national legal orders or at the international level. One might mention internal legislation such as the Dodd-Frank Act¹²⁹ or a global standard implemented by a coalition of governments, companies, and civil society such as the Extractive Industry Transparency Initiative. The EU has intervened in this field through

¹²² European Commission – Press release, Consultation on investment protection in EU-US trade talks, Strasbourg, 13 January 2015, at: http://europa.eu/rapid/press-release_IP-15-3201_en.htm.

¹²³ B. Kowalczyk-Hoyer, Promoting Revenue Transparency – 2011 Report on Oil and Gas Companies, p. 5, at: www.transparency.org/topic/detail/oil_and_gas.

¹²⁴ For an overview of the main instruments in the field see www.oecd.org/cleangovbiz/internationalconventions.htm

¹²⁵ Adopted by the General Assembly by resolution 58/4 of 31 October 2003, it has entered into force on 14 December 2005.

¹²⁶ See, however Art. X17 of CETA which reads 'For greater certainty, an investor may not submit a claim to arbitration under this Section where the investment has been made through fraudulent misrepresentation, concealment, corruption, or conduct amounting to an abuse of process'.

¹²⁷ These kind of clauses may as well be part of the definition of an investment. From the practical point of view, there is no difference between the two cases.

¹²⁸ In *Niko Resources (Bangladesh) Ltd. v. People's Republic of Bangladesh et al.*, ICSID Cases No. ARB/10/11 and No. ARB/10/18, the respondent based on the preservation of the integrity of the ICSID system and on the 'clean hands' doctrine its claim that the tribunal should decline its jurisdiction, underlining however that it was considering the agreements with the claimant still valid. This request was rejected by the tribunal. Another legal ground to reach the same outcome is the principle of *bona fide*, since a contract or a concession obtained by bribing public officials can hardly be deemed expression of good faith: *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24 (the claim was brought under the ECT, which does not refer to the laws of the host country, and at issue was the misrepresentation of Plama Consortium, an illegal but not corruptive act). Even if abundant, this case-law has its exceptions. For example, in 2007 a tribunal found that Georgia, the respondent, could not invoke the so called 'corruption defence' – i.e. to deprive an investment of the protection accorded by a BIT – since two presidents and two prime ministers had endorsed the agreements concerning oil pipelines and concluded on the basis of corruption. *Ioannis Kardassopoulos v. The Republic of Georgia*, ICSID Case No. ARB/05/18 (contra, see *World Duty Free Company Limited v. The Republic Of Kenya*, ICSID Case No. ARB/00/7: 'the Tribunal does not identify the Kenyan President with Kenya'. Of course, the degree of formality of the involvement of the State's representative may play a role).

¹²⁹ Dodd-Frank Wall Street Reform and Consumer Protection Act, at: www.sec.gov/about/laws/wallstreetreform-cpa.pdf.

some directives¹³⁰. In particular, the aim of the Accounting Directive is to raise international standards of transparency in the sector of extraction of oil, gas, mining and logging through the improvement of accountability, by allowing citizens in these countries to be informed about payments made by the companies to the government.

Moreover, in recent years, there has been a growing trend towards an increase in severity of national legislation against corruption. After the adoption of the US Foreign Corrupt Practices Act of 1977 (FCPA)¹³¹, some countries have criminalized the payment of bribes to other governments' officials in line with the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions and the United Nations Convention against Corruption. One of the main features of this anti-bribery legislation is that it tends to be applicable beyond borders with a significant extraterritorial reach. The UK Anti-Bribery Act, for instance, is applicable to the offence of failure to prevent bribery even if the conduct occurs outside the UK¹³². Along the same lines, the jurisdictional link in the FCPA has been interpreted loosely in the sense that even minimal acts such as using US email providers or telephone lines may be sufficient to establish a form of territorial jurisdiction¹³³. In this way, several prosecutions have been initiated in cases where the relevant conduct takes place abroad and anti-corruption legislation adopted at the national level is increasingly creating a level playing field for companies operating in the energy sector¹³⁴. Finally, another notable feature of the relevant legislation is that corporations may be held criminally responsible also for the conduct of agents and subsidiaries¹³⁵.

Against this background, it can be argued that a successful compliance strategy should be based on the adoption of preventive measures rather than remedial ones. In particular, with a view to adapting themselves to the applicable legal framework, thus avoiding time-consuming and costly prosecutions, companies should:

- Adopt anti-corruption guidelines and codes of ethics expanded not only to employees but also to business partners;
- Develop training programmes for employees so that they are constantly informed on the obligations provided for by the relevant legislation;
- Determine the risk posed by intermediaries through appropriate due diligence procedures;
- Consider that corporate self-reporting may be a relevant factor in the decision by key national authorities not to prosecute a case;
- Consider that compliance and reform efforts may be a critical factor for the decision of national authorities to enter into a deferred prosecution agreement or a non-prosecution agreement.

¹³⁰ Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013, Arts. 41 ff. See also for companies active in the extractive industries with securities admitted to trading on a regulated market the 'Transparency Directive' 2013/50/EU of the European Parliament and of the Council of 22 October 2013, in particular Art. 6.

¹³¹ Anti-Bribery and Books & Records Provisions of The Foreign Corrupt Practices, United States Code Title 15, Commerce and Trade Chapter 2B – Securities Exchanges, at: www.justice.gov/criminal/fraud/fcpa/docs/fcpa-english.pdf.

¹³² Sec. 12(5), Bribery Act 2010, at: www.legislation.gov.uk/ukpga/2010/23/pdfs/ukpga_20100023_en.pdf.

¹³³ The Criminal Division of the US Department of Justice and the Enforcement Division of the US Securities and Exchange Commission, *FCPA – A Resource Guide to the U.S. Foreign Corrupt Practices Act*, pp. 10-12, available at: www.sec.gov/spotlight/fcpa/fcpa-resource-guide.pdf.

¹³⁴ For an overview of FCPA cases initiated by the US Security and Exchange Commission, see: www.sec.gov/spotlight/fcpa/fcpa-cases.shtml.

¹³⁵ Sec. 8(3), Bribery Act 2010.

5 Energy related rules in DCFTAs and Energy Community

Energy represents one of the main challenges that Europe is currently facing¹³⁶. As shown in chapter 1, the EU is the third largest consumer of energy at the global level. The current demand for energy cannot be accommodated through an increase of domestic production, due to the limited energy reserves in the EU and the huge costs that that solution would imply. For this reason, Europe is highly dependent on energy imports.

Against this background, it is essential for the EU to preserve the stability and affordability of international supplies by establishing a dialogue with its suppliers, as well as with other countries and international organisations that play a major role in the energy field.

Among the various initiatives taken in the area, is the Energy Community Treaty, whose aim is to establish an integrated regulatory framework in the field of energy between the EU, South East Europe and the Black Sea region. Furthermore, in the framework of the Eastern Partnership, the EU has concluded Association Agreements establishing Deep and Comprehensive Free Trade Areas (DCFTAs) with Georgia, the Republic of Moldova and Ukraine, each containing a special chapter dealing with trade in energy. Other agreements are currently being negotiated with Morocco, Tunisia and Georgia.

The following sections will be devoted to the analysis of pending legal obligations under the frameworks of the Energy Community and the DCFTAs, as well as scrutinising their level of implementation and other outstanding issues.

5.1 The Energy Community

The Energy Community is an international organization established by means of an international treaty, signed in October 2005 in Athens and entered into force in July 2006¹³⁷. Parties to the Treaty are the EU, Albania, Bosnia and Herzegovina, Kosovo, the Former Yugoslav Republic of Macedonia, the Republic of Moldova, Montenegro, Serbia and Ukraine. Armenia, Georgia, Norway and Turkey only take part in the Energy Community as observers, and Georgia is expected to become a full-fledged member¹³⁸.

By signing the Energy Community Treaty, the contracting parties committed themselves to implement within specific deadlines core parts of the *acquis communautaire* on energy, i.e. to adopt specific regulatory frameworks concerning, among other issues, electricity, gas and oil. The latest obligations under the Energy Community Treaty concerning electricity, gas and oil are the following:

- **Acquis on electricity.** As of 1 January 2015 the deadline for the implementation of the whole Third EU Energy Package has expired. The contracting Parties were bound to implement the provisions of Directive 2009/72/EC, setting out rules for the generation, transmission, distribution and supply of electricity and laying down consumer rights and service obligations¹³⁹, and Regulation (EC) 714/2009, setting out common provisions on cross-border exchanges and dealing also with competition issues¹⁴⁰.
- **Acquis on gas.** 1 January 2015 marked the deadline for the implementation of Directive 2009/73/EC, aiming at the introduction of common rules for the transmission, distribution, supply and storage of

¹³⁶ See Chapter 1.

¹³⁷ The Consolidated version of the Treaty establishing the Energy Community is available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/2796177/Pages_from_2178178.pdf.

¹³⁸ Georgia was expected to join the Energy Community by October 2014. However, negotiations are now suspended and it is not clear when Georgia will accede to the Treaty. See <http://weg.ge/wp-content/uploads/2014/11/EC-Just-en1.pdf>.

¹³⁹ Directive 2009/72/EC concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC.

¹⁴⁰ Regulation (EC) No 714/2009 on conditions for access to the network for cross-border exchanges in electricity and repealing Regulation (EC) No 1228/2003.

natural gas¹⁴¹ and Regulation (EC) No 715/2009¹⁴², setting out provisions concerning natural gas transmission networks, gas storage and liquefied natural gas facilities.

- **Acquis on oil.** The pending obligation, expiring on 1 January 2023, concerns the transposition of Directive 2009/119/EC, that obliges the Parties to ensure that a minimum amount of emergency oil stocks¹⁴³.

The *acquis* to be implemented is nonetheless in constant development and the decision to incorporate a new *acquis* is taken by the Ministerial Council of the Energy Community on the basis of a proposal by the European Commission¹⁴⁴.

5.2 DCFTAs with Georgia, the Republic of Moldova and Ukraine

On 27 June 2014, the EU signed Association Agreements with Georgia, the Republic of Moldova and Ukraine¹⁴⁵. This took place in the framework of the Eastern Partnership, whose aim is to establish closer ties between Europe and its Eastern neighbours, by creating deep political and economic associations capable of supporting the political stability and economic prosperity of those countries, which are a matter of concern for the EU itself.

The AAs with Georgia, the Republic of Moldova and Ukraine include a DCFTA that aims at opening up markets by progressively removing obstacles such as customs duties and quotas, and harmonizing trade-related rules in several sectors, in order for associated countries to gradually come into line with EU standards.

The DCFTA also include ad hoc provisions on issues concerning trade in energy¹⁴⁶, which can be divided into four categories.

- **Rules concerning the pricing of energy goods.** In the AAs, Parties agree that the price for the supply of gas and electricity for non-household customers shall be determined solely by supply and demand, with a view of letting market price prevail¹⁴⁷. A derogation to this rule can be justified¹⁴⁸ only by reasons of general economic interest¹⁴⁸. In addition, Parties are prohibited from applying dual pricing¹⁴⁹.
- **The establishment of an independent regulator.** Linked to the obligations concerning pricing of energy goods is the commitment of the Parties to designate a regulatory authority charged with ensuring effective competition and an efficient functioning of the gas and electricity markets. Such an authority is to be legally distinct and functionally independent from any other public or private

¹⁴¹ Directive 2009/73/EC concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC.

¹⁴² Regulation (EC) No 715/2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) No 1775/2005.

¹⁴³ Directive 2009/119/EC imposing an obligation on Member States to maintain minimum stocks of crude oil and/or petroleum products.

¹⁴⁴ For a detailed overview of the *acquis* currently in force and the implementation deadlines, see the Energy Community Legal Framework, third edition 2013, (consolidated version), available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/2178178/EC_Legal_Framework_WEB.pdf.

¹⁴⁵ Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and Georgia, of the other part; Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and the Republic of Moldova, of the other part; Association Agreement between the European Union and its Member States, of the one part, and Ukraine, of the other part.

¹⁴⁶ See Title IV, Chapter 11 of the AAs with Georgia and Ukraine and Title V, Chapter 11 of the AA with Moldova.

¹⁴⁷ See Articles 216(1) AA with Georgia, 346(1) Moldova, 269(1) Ukraine.

¹⁴⁸ See Articles 216(2) AA with Georgia, 346(2) Moldova, 269(2) Ukraine. The agreements with Ukraine and Moldova specify that the expression 'general economic interest' is to be interpreted in the same sense as it is understood in Article 106 of the TFEU and in particular in accordance with the case law of the Court of Justice of the EU.

¹⁴⁹ See Chapter 3.2.

entity¹⁵⁰. Its decisions shall be impartial with respect to all market participants, and any operator affected by such decision shall have the right to appeal before an independent body¹⁵¹.

- **Transit and transport of energy goods.** Parties are bound to ensure the transit of energy goods across their territory, in accordance with their international commitments under the GATT and the Energy Charter Treaty¹⁵². They cannot interfere with the transit of energy goods, except where such interference is specifically provided for in a contract or other agreement¹⁵³. Parties are also bound to ensure that operators take the necessary measures to minimise the risk of interruption or reduction of transit and swiftly restore its operation in the case of failure¹⁵⁴. In addition, they shall take all necessary measures to prohibit and address any unauthorised taking of energy goods in transit through their territory¹⁵⁵. In order to reduce the risk of an abrupt halt in transit of energy goods, the agreements provide that in the event of a dispute over any matter involving the Parties or an entity subject to their control or jurisdiction, Parties are prohibited from interrupting or reducing – and from permitting any entity to interrupt or reduce – the transit of energy goods prior to the conclusion of a dispute resolution procedure¹⁵⁶. To this effect, all agreements provide for a dispute resolution mechanism and, in particular, for a fast-track dispute settlement procedure for urgent energy disputes¹⁵⁷. Furthermore, they envisage an early warning mechanism¹⁵⁸ aiming at preventing and rapidly reacting to an emergency situation¹⁵⁹ or to a threat concerning the supply and demand of natural gas, oil or electricity.
- **Access to the exploration and production of hydrocarbons.** Considering the significant Ukrainian reserves of hydrocarbons, the AA with Ukraine also contains a set of provisions concerning access to the exploration and production of gas and oil. In particular, after recalling the right of each Party to determine the areas available for the exercise of the activities of prospecting, exploring for and producing hydrocarbons, the AA provides that whenever a geographical area is made available for such activities, each Party shall provide access and licensing to entities from all Parties on a non-discriminatory basis¹⁶⁰.

¹⁵⁰ See Articles 215(1) and 216 AA with Georgia, 353(1)Moldova, 277(1)AA Ukraine.

¹⁵¹ See Articles 215(2)(3) AA with Georgia, 353(2)(3)Moldova, 277(2)(3)Ukraine.

¹⁵² See Articles 211AA with Georgia, 348 Moldova, 272 Ukraine. See also Articles V.1, V.2, V.4 and V.5 of GATT 1994 and Articles 7.1 and 7.3 of the Energy Charter Treaty.

¹⁵³ See Articles 21(1) AA with Georgia, 350(1) Moldova, 276(2)Ukraine. In the case of the AA with Georgia, Parties are allowed to intervene also 'where a continued operation of the energy transport facilities without prompt corrective action creates an unreasonable threat to public security, cultural heritage, health, safety or the environment'.

¹⁵⁴ See Articles 214 AA with Georgia, 352 Moldova, 276(1) Ukraine.

¹⁵⁵ See Articles 212 AA with Georgia, 350 Moldova, 275 Ukraine.

¹⁵⁶ See Articles 213(2) AA with Georgia, 350(2) Moldova, 276(2) Ukraine.

¹⁵⁷ See Articles 252 AA with Georgia, 388 Moldova, 309 Ukraine. The agreements are aiming at establishing a certain legal framework to deal with energy disputes in a timely and effective manner, before a halt in energy transit is performed. The aim of such a framework is to avoid situations such as the Ukraine gas crisis of 2006 and 2009, where the solution of the dispute, after an abrupt halt in gas transit, was left to intergovernmental negotiations only. It is to be noted that the infringement of the provisions concerning transit of energy goods and dispute settlement does not give rise to specific sanctions under the agreement, so the liability of the parties is governed by international law.

¹⁵⁸ See Annex XVIII AA with Georgia, Annex XXXI Moldova, Annex XXVI Ukraine.

¹⁵⁹ Emergency is qualified as 'a situation causing a significant disruption or a physical interruption of supply of energy goods'. Cfr. The preceding note.

¹⁶⁰ See Articles 279 and 280 AA with Ukraine. Following the annexation of Crimea to Russia, the existing demarcation lines between the littoral States involved are at stake. Should Crimea be considered Russian territory, a huge part of the Black Sea waters will not be available for exploration and production of hydrocarbons on the part of Ukraine and the EU.

5.3 The implementation of energy related provisions within the Energy Community and DCFTAs and the outstanding issues

Having outlined the legal framework and the obligations resulting from the Energy Community Treaty and the DCFTAs, this section offers a country-based overview of the level of implementation of energy related provisions in Albania, Bosnia and Herzegovina, Georgia, Kosovo, the Former Yugoslav Republic of Macedonia, the Republic of Moldova, Montenegro, Serbia and Ukraine.

- **Albania.** The Albanian legal framework concerning electricity is largely non-compliant with the *acquis communautaire*, due to insufficient unbundling, lacking of provisions concerning third party access, inappropriate criteria for eligibility and lack of transposition of the requirements concerning balancing and customer protection. In the field of gas, Albania has developed a legal framework which seems to be suitable for the future development of its gas infrastructure, in particular in view of the construction of the Trans-Adriatic Pipeline, which will connect Albania to Greece and Italy. As regards the oil sector, Albania is currently in the process of redesigning its emergency stockholding system¹⁶¹.
- **Bosnia and Herzegovina.** The status of compliance of Bosnia and Herzegovina with regards to its obligations under the Energy Community treaty is highly unsatisfactory and studded with serious infringements. The electricity and the gas market are underdeveloped and suffer from a lack of implementation of most of the basic rules set out in the EU *acquis*. Huge reforms are needed to put the country in line with its obligations. Furthermore, Bosnia and Herzegovina has no national legislation on compulsory stocks of oil¹⁶².
- **Georgia.** Georgia is currently working in preparation of its upcoming accession to the Energy Community. In the field of electricity, some of the EU requirements are already met, but effective unbundling still needs to be implemented, while market opening should be accelerated. Unbundling is also still an open problem in the field of gas¹⁶³.
- **Kosovo.** The level of implementation of the EU *acquis* on energy in Kosovo inevitably suffers from the difficult political situation that the country is experiencing. Several legal measures have been adopted, but they still need to be implemented. As to the electricity sector, the main problems concern compliance with the unbundling requirements, market opening and price regulation. As far as gas is concerned, it must be noted that there is no gas market in Kosovo at the moment. However, in view of the future participation of the country in regional gas penetration initiatives, authorities are working to fully implement the Third energy Package. As to oil, Kosovo is to start working on a draft law on emergency oil stocks¹⁶⁴.

¹⁶¹ See Energy Community Secretariat, Albania Country Report, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356147/EC_Implementation_Report_2014_ALBANIA.pdf.

¹⁶² See Energy Community Secretariat, Bosnia and Herzegovina Country Report, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356150/EC_Implementation_Report_2014_BOSNIA_AND_HERZEGOVINA.pdf.

¹⁶³ N. Sumbadze, Possible Challenges of harmonization of Georgian Legislation with the *Acquis Communautaire* of the European Union in Energy sector, PMC Research Center and Konrad Adenauer Foundation, available at: http://www.kas.de/wf/doc/kas_39854-1522-1-30.pdf?141208103512.

¹⁶⁴ See Energy Community Secretariat, Kosovo Country Report, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356151/EC_Implementation_Report_2014_KOSOVO.pdf

- **The Former Yugoslav Republic of Macedonia.** The Former Yugoslav Republic of Macedonia has adopted several effective reforms to meet with EU standards on energy. In the field of electricity, the country is compliant with most of the EU *acquis*, although unbundling, market opening and price regulation still need to be dealt with further. In the gas sector, the country has to address some shortcomings, especially as to unbundling. With regard to oil, Macedonia is working on the transposition of the provisions concerning compulsory oil reserves¹⁶⁵.
- **The Republic of Moldova.** As to the electricity sector, the Republic of Moldova still falls shortly of a proper implementation of the EU *acquis*, not only as to the Third, but also as to the Second Energy Package. Authorizations for new power plants, unbundling, and third party access have been addressed by law but implementing measures have not been adopted yet. Market opening and price regulation are still open issues. The same considerations apply to the gas sector. As to oil, no initiatives have been taken to start the transposition of the obligations concerning emergency stockholding¹⁶⁶.
- **Montenegro.** Montenegro has adopted a good quality reform for the energy markets, which is currently being implemented. Further efforts are required as to unbundling and market opening. Montenegro has currently no gas market, but initiatives for gas penetration in the region are being developed and the legal national framework is mostly in line with the *acquis*. As to oil, the country is working on the establishment of emergency oil stocks¹⁶⁷.
- **Serbia.** Serbia has performed well in the implementation of the provisions concerning the electricity market. The reform of the sector is mostly in line with the requirements of the EU *acquis*. Further efforts are required towards a full market opening, in particular as to price regulation. With regard to the gas market, the legal framework is mostly in line with the requirements of the *acquis*, although is not being effectively enforced. The main issues concern unbundling, third party access, market opening and balancing. As to oil, Serbia has started to work towards complying with the requirement concerning emergency stocks¹⁶⁸.
- **Ukraine.** In the area of electricity, Ukraine is currently undergoing a process of renovation of the market model that is expected to become fully operational only in July 2017. The work towards a complete liberalization of the market is still ongoing and the role of the regulatory authority needs to be reinforced. At the moment, the country is largely in a state of non-compliance with the EU *acquis*, due to a partial transposition of unbundling, third party access and consumer protection requirements. As to gas, the unbundling of energy production and supply has not yet been implemented: market opening, price regulation and security of supply are still not properly

¹⁶⁵ See Energy Community Secretariat, Former Yugoslav Republic of Macedonia Country Report, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356154/EC_Implementation_Report_2014_FYR_of_MACEDONIA.pdf.

¹⁶⁶ See Energy Community Secretariat, Moldova Country Report, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356155/EC_Implementation_Report_2014_MOLDOVA.pdf.

¹⁶⁷ See Energy Community Secretariat, Montenegro Country Report, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356158/EC_Implementation_Report_2014_MONTENEGRO.pdf.

¹⁶⁸ See Energy Community Secretariat, Serbia Country Report, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356161/EC_Implementation_Report_2014_SERBIA.pdf.

addressed by legislation. With regards to oil, Ukraine has not yet started working on the requirements concerning emergency stockholding¹⁶⁹.

In conclusion, most Parties to the Energy Community and associated countries have managed to adopt legally binding measures to transpose their legal obligations concerning the energy sector, but failed to implement them or to effectively enforce the redesigned legal framework.

The efforts towards the creation of open energy markets in line with EU standards is still ongoing and progress is being made. Most countries have shown a serious commitment in advancing the effective implementation of the EU *acquis*, and the bodies of the Energy Community are providing all necessary assistance towards that end¹⁷⁰.

6 General conclusion

European States are undergoing a long-term energy transition towards a low-carbon economy, where renewable sources are expected to play a central role in the energy mix. Nonetheless, in the coming decades fossil fuels will continue to account for a large share of final consumption and they will be increasingly imported. Therefore, the capacity of securing energy supplies while respecting relevant legal obligations represents a priority for the European decision-makers, both at national and EU level.

In the energy policy, the EU shares the legal competence with Member States and recognizes their autonomy in choosing their own energy mix and their control over primary energy sources. A consequence of this legal arrangement is the limited scope for European initiatives in terms of security of supply that go beyond the completion of the internal market and the development of infrastructures and interconnections. However, the recent crisis between Russia and Ukraine has once again highlighted the importance of cooperation of Member States and the external dimension to energy policies due to the structural condition of net energy importer of the EU.

Proposals for building an Energy Union have been put forward and a significant debate has followed, with a Communication delivered at the end of February by the Commission and recently discussed by the European Council. Central to this political project are trust and solidarity among Member States, which imply a larger role for European institutions. Nonetheless, as the conclusions of the European Council show, it is difficult to foresee in the near future the adoption of innovative policy proposals such as the introduction of a single gas buyer or a European supervisor for intergovernmental agreements.

When the legal regulation of energy issues comes to play, a very fragmented and intricate landscape emerges. Quite often various treaties (bilateral and multilateral ones) deal with the same subjects; the same end (e.g., the support of renewable energy sources) may sometimes be attained in different ways, both legal and illegal; finally, there are practices (like dual pricing) covered by many different rules and whose legal status cannot be easily assessed. In few words, international trade law is not a fully consistent and complete whole. In order to clarify some parts of the WTO law and to fill some of its lacunae, the European Union has recently negotiated a series of comprehensive free trade agreements with many important commercial partners, in North America as well as Eastern Europe. These treaties, which also cover the field of investment in the energy sector, sometimes provide for an investor-State dispute settlement mechanism that might limit the regulatory autonomy of European Member States to the advantage of corporations.

¹⁶⁹ See Energy Community Secretariat, Ukraine Country Report, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356163/EC_Implementation_Report_2014_UKRAINE.pdf.

¹⁷⁰ See Energy Community Secretariat, Annual Implementation Report, 2014, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/3356393/Energy_Community_Implementation_Report_2014_WEB.pdf.

The EU has also taken several international initiatives meant to preserve the stability and affordability of international supplies, such as the conclusion of the Energy Community Treaty and Association Agreements with Georgia, the Republic of Moldova and Ukraine. These initiatives are aimed at establishing an open energy market in line with the EU standards, by encouraging the parties involved to implement core parts of the *acquis communautaire* on energy.

Although most of the EU counterparts have successfully adopted legally binding measures to transpose their legal obligations concerning the energy sector, the efforts towards the creation of integrated regulatory framework is still ongoing. In fact, despite great progress, several countries are still non-compliant with their legal obligations, in particular when it comes to the implementation and enforcement of the recently introduced rules. However, most of them have shown a serious commitment in advancing the effective implementation of the EU *acquis*, and the institutions of the Energy Community are providing all necessary assistance.

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